The Economist

DECEMBER 17TH–23RD 2005 www.economist.com

Japanese innovation is back
PAGES 59-61

The rush to invest in India
PAGE 63

Battle for the London Stock Exchange
PAGES 11 AND 64

America goes off the death penalty
PAGES 10 AND 39

How to deal with Iraq's insurgents

ONLINE FEATURES
Cities Guide Go
Country Briefings Go
Audio interviews Go
Classifieds Go

PRINT EDITION

Full contents
Enlarge current cover
Past issues/regional covers

GLOBAL AGENDA
POLITICS THIS WEEK
BUSINESS THIS WEEK
OPINION
Leaders
Letters
WORLD
United States
The Americas
Asia
Middle East & Africa
Europe
Britain
Country Briefings
Cities Guide
SURVEYS
BUSINESS
Management Reading
Business Education
Executive Dialogue
FINANCE & ECONOMICS
Economics Focus
Economics A-Z
SCIENCE & TECHNOLOGY
Technology Quarterly
PEOPLE
Obituary
BOOKS & ARTS
Catch if you can
Style Guide
MARKETS & DATA
Weekly Indicators
Currencies
Big Mac Index
DIVERSIONS
RESEARCH TOOLS
CLASSIFIEDS
DELIVERY OPTIONS
E-mail Newsletters
Mobile Edition
RSS Feeds
The Economist Group
Economist Intelligence Unit
Economist Conferences
The World In
Intelligent Life
CFO
Roll Call
European Voice
Economist Diaries and Business Gifts

Print Edition
December 17th 2005

On the cover
The Iraqi insurgency is not much about al-Qaeda, and a lot about the Sunni Arab minority's resentment at being marginalised. That's why the Shias need to make more effort to accommodate the Sunnis: leader

Previous print editions
Dec 10th 2005
Dec 3rd 2005
Nov 26th 2005
Nov 19th 2005
Nov 12th 2005

More print editions and covers »

Subscribe
Subscribe to the print edition
Or buy a Web subscription for full access online
RSS feeds
Receive this page by RSS feed

The world this week
Politics this week
Business this week

Leaders
Iraq's general election
How to deal with Iraq's insurgents

Intellectual property
The real lesson of BlackBerry

The death penalty
After Tookie

London Stock Exchange
Clara's difficult Christmases

The pecking order
Runner-up, up and away

Letters
On Xinjiang, Italy, fat animals, the Balkans, pensions, snow, football

Special Report
American military tactics
How to do better

United States
A new front in the culture wars
The Lord's word

The death penalty
Tookie v Arnold

Richard Pryor
Rebel with a cause

The Patriot Act
Of liberty and libraries

Litigation and health care
Scalpel, scissors, lawyer

Lexington
A wise man in Washington

The Americas
Bolivia
A champion of indigenous rights—and of state control of the economy

Peru
Rise of another outsider

Cuba
An unsilenced voice for change

Canada
Worm in the bud

Asia
Japan's economy
Land of the rising price

East Asian diplomacy
Dead on arrival

China
A demo turns bloody

Australia
On the beach

Business
India
The next wave

Information technology
Digital dragon

Obesity and advertising
Junior fat

Coke v Pepsi
Things go worse with Coke

Corporate tax
Sighs of relief

American multinationals
Stars and stripes for ever

The film industry
End of the dream

Videoconferencing
The Halo effect

Face value
Firefox swings to the rescue

Special Report
The future of Japanese business
Competing through innovation

Finance & Economics
Private equity in Germany
Anglo-Saxon attitudes

Stock exchanges
All roads lead to London

A Japanese trading debacle
Please may I take it back?

Legg Mason
Its biggest bet yet

Microcredit and disasters
Starting over

Oil prices
Decisions and dilemmas

Preparing for catastrophe
Bunker mentality

Economics focus
Middle-age spread

Science & Technology
Climate change
Pricing the global conscience

Predicting earthquakes
Granite batteries

Planet-hunting
ESP for ESPs

Skiing
Not waxing lyrical

Books & Arts
Online gaming
Worlds without end

Popularising philosophy

Advertisement

After the horror, more horror

Thailand
The oracle of Lumpini park

Middle East & Africa

Syria and Lebanon
The Syrians are in the dock, but the murders continue

Iraqi Kurdistan
Taking the oil

Iran
Sex rears its head

Israel's Supreme Court
Who should make the law?

Ethiopia and Eritrea
Big brother has other worries

Somalia
A state of utter failure

Europe

France and immigration
After the riots

Balkan history
A better view of the bad guys

The Balkans and Europe
Testing times

Germany and Russia
Jobs in the pipeline

Italy's high-speed train link
Boring through the Alps

Belarus
Turning the screw

Charlemagne
A modest proposal

Britain

The police
Boys in blue

Politics
Lib Dem rumblings

Evidence under torture
The fruit of the poisoned tree

School reform
Sorting out schools

Airports
Headwinds

Ranking public services
Made to measure

Banking competition
Another day, another probe

Bagehot
The good European

Articles flagged with this icon are printed only in the British edition of *The Economist*

Question marks

American 20th-century writing
Sharp-tongued woman

Terror in South-East Asia
Nailing a bombing

Conducting
Maestra Marin

Obituary

Obituary
Eugene McCarthy

Economic and Financial Indicators

Overview

Output, demand and jobs

Prices and wages

Retirement saving

Money and interest rates

The Economist commodity price index

Stockmarkets

Trade, exchange rates and budgets

Government budget balances

Emerging-Market Indicators

Overview

Hourly compensation

Economy

Financial markets

Advertisement

Classifieds

Jobs
Call for Candidatures The Anna Lindh Euro-Mediterranean Foundation for the Dial....

Business / Consumer
Business Opportunity - WSI Internet Start Your Own Busines....

Tenders
CALL FOR EXPRESSION OF INTEREST (EOI) BENEFICIARY COUNTRY....

Jobs
CARE Canada seeking senior development/relief professionals for Country Director positions.....

Tenders

Jobs
Shaping policy in the world's largest mobile telecommunication company Attractive s....

Sponsors' feature

Copyright © The Economist Newspaper Limited 2005. All rights reserved. | Legal disclaimer | Accessibility | Privacy policy | Terms & Conditions | Help

Politics this week

Dec 14th 2005
From The Economist print edition

Reuters

Amid suicide-bombs and more revelations of mistreatment of Sunni prisoners by militias loyal to the Shia-led government, **Iraqis** prepared to vote for more than 200 parties in a general election on December 15th to usher in a four-year parliament under a new constitution. See article

A UN-appointed prosecutor, Detlev Mehlis, issued a second report saying that more evidence implicated **Syria's** government in the murder of Rafik Hariri, a former prime minister of **Lebanon**, in February. Mr Mehlis suggested extending the inquiry by six months. In the latest of a series of murders in Lebanon, a leading anti-Syrian editor and MP, Gibran Tueni, was killed by a car bomb. Many prominent Lebanese immediately blamed Syria. See article

Iran's president, Mahmoud Ahmadinejad, said on television that the Holocaust was a myth held to be "higher than God himself" and repeated calls for Israel to be moved to Europe or America. An Israeli spokesman described the comments as a "perverse vision of the world".

Human Rights Watch, a New York-based group, named senior Sudanese officials, including the president, who, it said, should be investigated for crimes against humanity in **Darfur.** More than 200,000 people have been killed in the province since 2003.

Kenya's president, Mwai Kibaki, swore in a new cabinet, though many original nominees refused to accept posts. Mr Kibaki sacked his entire previous cabinet after losing a constitutional referendum.

Chad upset the World Bank by going back on a deal it made two years ago to devote most of its new oil revenues to reducing poverty in exchange for the Bank's investment in a pipeline to export the oil. Chad's government now wants to use the money for military spending and government salaries.

Pre-positions

More wrangling took place ahead of the **European Union summit**, with France and other countries demanding deeper cuts in Britain's budget rebate. The French also put on hold plans to give Macedonia the status of candidate for accession to the EU. See article

The former German chancellor, **Gerhard Schröder**, ran into heavy criticism for taking a job as chairman of a consortium building a pipeline from Russia to Germany, agreed on when he was chancellor. See article

An investigation by the Council of Europe into allegations of secret **CIA prisons in Europe** found preliminary evidence that agents had kidnapped and illegally transferred suspects between

countries.

French police arrested 20 Islamic radicals in the Paris region who they said were part of a network linked to “a terrorist enterprise”. Most of the suspects were of north African origin or descent.

Back to the ballot box

Michelle Bachelet, the presidential candidate of **Chile's** ruling centre-left Concertación coalition, faces a tight run-off election against Sebastián Piñera, a moderate conservative. In the first round on December 11th, Ms Bachelet won 46% of the vote, against a combined 48% for the two conservative candidates.

A court in **Brazil's** Amazon state of Pará found two local men guilty of the killing last February of Dorothy Stang, an American nun and environmental activist. Two ranchers have been accused of ordering the crime.

Colombia's president, Álvaro Uribe, offered to withdraw troops from a small mountain town to allow talks with FARC guerrillas over the release of dozens of hostages. The government was also to start talks with the smaller ELN guerrilla army.

The United Nations **climate-change** conference in Montreal ended more positively than some had predicted. The United States agreed to join talks in the future, as long as mandatory emissions targets were not on the agenda. See article

Talking Doha down

AFP

The **World Trade Organisation's** biennial ministerial conference got under way in Hong Kong, amid protests and scuffles with the police. Cold water has been poured on any hope of substantive deals on free trade in farm goods, industrial tariffs and services emerging from the talks. See article

Chinese police fired on a demonstration in a Guangdong village, killing three people (according to officials) or 20 (according to the villagers). Unusually, the government promptly announced that the official responsible had erred and would be tried. See article

Eleven members of **India's** parliament were filmed by a news website allegedly receiving cash for asking parliamentary questions. Nine of them have been suspended.

Cronulla, a beach suburb of **Sydney**, experienced two nights of violence after a group of young Lebanese men attacked lifeguards. Thousands of white Australians then went on a racist rampage. See article

A row over death row

Stanley “Tookie” Williams, who co-founded the infamous Crips gang in the 1970s, was executed in **California**. Mr Williams had turned into an advocate against gang culture and written books for

children. Governor Arnold Schwarzenegger refused to exercise clemency, pointing out that Mr Williams had never accepted responsibility or expressed regret for four brutal murders of which he was found guilty in 1981. See article

Louisiana's governor, Kathleen Blanco, postponed next year's **New Orleans** mayoral election indefinitely. Ms Blanco says the city has still not sufficiently recovered from Hurricane Katrina. Meanwhile, George Bush strongly rejected claims that the government's inadequate response to the disaster in late August was based on race.

The Supreme Court said it would hear a case that challenges the constitutionality of **Texas's** congressional boundaries. Democrats claim that a contentious redistricting map, overseen by Tom DeLay, the suspended majority leader of the House of Representatives, gave the Republicans several extra seats in the 2004 congressional elections.

Virgin Galactic, a space-tourism firm created by Sir Richard Branson, announced an agreement with **New Mexico** to build a spaceport in the state. Flights are scheduled to take off in 2008 from the complex, which will be near the town of Truth or Consequences.

AFP

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Business this week

Dec 14th 2005
From The Economist print edition

ConocoPhillips launched a $35.6 billion cash-and-shares takeover bid to buy **Burlington Resources**, another energy company based in Houston. Burlington specialises in using new technologies to drill for natural gas, which has recently been trading at record highs. See article

Paramount Pictures agreed to buy **DreamWorks SKG**, the film studio created by Steven Spielberg, Jeffrey Katzenberg and David Geffen, for $1.6 billion including debt. The deal is a blow to NBC Universal, which had been in takeover talks with DreamWorks and is now expected to lose lucrative distribution contracts for its films outside America and DVDs worldwide. See article

Pernod Ricard sold its **Dunkin' Brands** unit to three private-equity firms for $2.4 billion. The unit's franchises include the Dunkin' Donuts coffee shops, which will be developed as a low-cost alternative to Starbucks.

PepsiCo's stockmarket value overtook **Coca-Cola's** for the first time on December 12th. PepsiCo has diversified its brand over the years with beverages, such as Gatorade and Tropicana, that are perceived as relatively healthy. The firm, which has seen its share price rise by 14% this year, now gets only 20% of its revenue from carbonated soft drinks, compared with Coca-Cola's 80%. See article

The benefit of hindsight

Steve Case, who recently resigned from **Time Warner's** board, admitted that the merger with AOL had been wrong and called for the company to be split up. Mr Case had attracted severe criticism as an architect of the merger from a group of dissident investors who want the media conglomerate to take remedial action, such as selling AOL. Mr Case's admission adds to the pressure on Time Warner's directors, who are reportedly considering an alliance between AOL and either Google or Microsoft.

Standard & Poor's cut its credit-rating for **General Motors** by two notches and gave its starkest warning yet that the beleaguered carmaker will eventually file for bankruptcy protection. Meanwhile, GM said it had not reached an agreement with Tracinda, Kirk Kerkorian's investment firm which owns nearly 10% of GM, to appoint Jerome York, a Kerkorian lieutenant, to its board. Talks are to continue “in the future”.

NTP rejected an offer by **Research In Motion**, the makers of BlackBerry wireless devices, to settle their long-running patent dispute. Without an agreement, RIM faces an injunction that could shut down its service in the United States. See article

Vodafone won an auction to buy **Telsim**, Turkey's second-largest mobile-phone operator, by agreeing to pay £2.5 billion ($4.6 billion). Vodafone expects demand for mobile phones in Turkey to surge—the country is forecast to have a larger population than Germany's by 2017.

Electronic Arts, a video-game developer, offered to buy **JAMDAT**, a firm that specialises in

creating games for mobile phones, for $680m. The deal comes amid a rapid expansion in mobile gaming, which is estimated to be worth $2 billion worldwide in 2005 compared with $1 billion in 2004.

Bonus

Lehman Brothers led a crop of stellar results from Wall Street investment banks. In the year ending November 30th, the firm's net income rose by 38% on the previous year, to $3.3 billion.

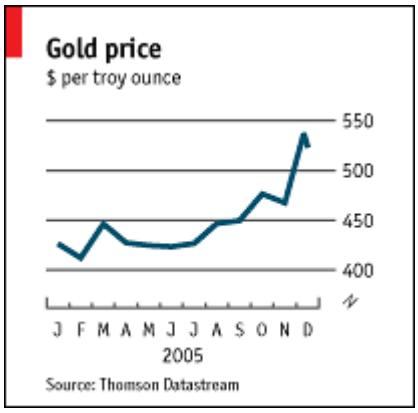
The first federal court case brought against **Merck** over Vioxx, an anti-inflammatory drug that was withdrawn on safety grounds, ended in a mistrial after the jury failed to reach a unanimous decision (two state cases have already been heard). The judge ordered the case to be retried. See article

The OECD reported that China had surpassed the United States for the first time in exporting **information-technology goods**, such as computers, mobile phones and related parts. China exported $180 billion-worth of IT goods in 2004, and is expected to keep its top position when figures are collated for 2005. See article

America's Federal Reserve put up its key **interest rate** by one-quarter of a percentage point, for the 13th consecutive time, to 4.25%. Economists pored over the language of the central bank's accompanying statement for an indication that the cycle of interest-rate rises will soon end.

Showing its mettle

The price of **gold** continued its bullish run, breaking $540 a troy ounce for the first time since 1981 during trading on December 12th. Japanese investors, looking for higher-yielding assets than the weakened yen, are reckoned to have been a primary factor in the recent price hike. But some analysts also predict the price will remain high next year, as big gold producers have lowered forecasts of their output.



Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com OPINION

Iraq's general election

How to deal with Iraq's insurgents

Dec 14th 2005
From The Economist print edition

This week's election is a great chance for Iraq, if the Shia and Kurdish victors are willing to be generous

Eyevine

IRAQ is a bloody mess, and will stay that way for quite some time. It is nothing like George Bush—or, for that matter, *The Economist*—hoped it would become when he sent in his troops nearly three years ago to get rid of Saddam Hussein. This week's general election will not turn things round overnight. But the election of a representative government offers Iraqis a chance to start slowly to stem the tide of mayhem and murder. For some time to come, America and its dwindling band of allies will have to underpin the new order's fragile security with military forces. But it will take more than American staying power to give Iraqis a decent, secure state. Almost everything now depends on their own desire for internal reconciliation, and their willingness to make sacrifices in order to achieve it.

Hope springs eternal

To be sure, there has already been a string of hopeful political events in the past year. Last January, Iraqis stunned the world by turning out in remarkable numbers to vote for an interim government. In October, they endorsed a new constitution. And this week they will vote for a four-year parliament that will embrace a much wider range of Iraqis, including a fair number of Sunni Arabs (20% or so of the population) as well as the already dominant Shia Arabs (60%) and the doggedly autonomous Kurds (20%). Last time, in January, the Sunni Arabs abstained en masse. This time many more seem set to vote, and are sure to win much fairer representation under a new electoral system. That inspires hope too. But hope has been dampened by the failure of genuine advances in democracy to make Iraq any safer for its hapless people.

The insurgency has refused to abate, even if it has not actually got stronger. This suits the

insurgents fine. The longer the mayhem continues, the likelier the new order is to disintegrate, whatever the merits of the new constitution and however representative the new parliament. And the longer the insurgency grinds on, the likelier it is that the Americans, even under a stubborn Mr Bush, will lose their nerve and depart. Guerrillas the world over win merely by not losing. It is plain, despite improvements in American counter-insurgency techniques (see article), that military power cannot alone defeat the insurgents. Iraq will never function as a secure state until a critical mass of Sunni Arabs are persuaded that it is in their interest to help put down the insurgents.

But how? American military power, gradually replaced by Iraqi forces, may be able to keep the insurgency at bay; but it can be defeated, or at least isolated, only by political means.

Official Washington has stuck for too long to the line that the insurgents are mostly jihadists linked to al-Qaeda and “regime remnants” intent only on reclaiming their former privileges. It has been convenient for both the Bush administration and for Iraq's interim government to portray things that way; but, if it was ever true, it no longer is. The insurgency now has a broad base within the Sunni population, much of which was traumatised by the sweeping away of the Baathist state and the erasure of its key institutions, notably the army. In many Sunni minds, Mr Hussein's dictatorship is being replaced by a Shia dictatorship. The Shias may be the majority but are held to be carving a proud Arab nation into one oil-rich Shia state under the influence of Iran, and a separate breakaway region, also rich in oil, for the Kurds. If the post-Saddam dispensation is to be winner-takes-all, Sunnis seem determined to make sure that there will be no winner at all.

The new parliament's first job must therefore be to create a coalition government broad enough to persuade the Sunnis that they will have a central, if no longer dominant, place in the new Iraq. The United Iraqi Alliance, a predominantly Shia Islamist collection implicitly blessed by the hugely influential Grand Ayatollah Ali al-Sistani, looks set to win the most votes. An alliance of the two main Kurdish parties is even surer to sweep the Kurdish north. Together, these two blocks have the numbers to run the show, as they have done for the past year. But it is crucial that they now embrace at least one of the Sunni-led alliances that have emerged since January.

This will not be an easy thing for Shias and Kurds to do. Many feel that they owe the Sunnis nothing after years of oppression at their hands. But taking Sunni parties into a governing coalition is only the first of several difficult steps the former underdogs need to take if they are to draw the sting of the insurgency. They will also have to make real concessions, even if this means tweaking the new constitution. Though the document has many merits, and was negotiated painstakingly, its formula for sharing Iraq's oil revenues is divisive, making Sunnis fear they will not get a fair whack. And parliament should limit a provision that enables the Shia Arabs to create a “super-region” of perhaps eight or nine provinces. As it stands, this lets Sunnis believe that federalism means breaking up the country. Parliament should also soften the deBaathification rules, so that many more Iraqis who served Mr Hussein's dictatorship should be drawn back into the machinery of state, unless they are senior figures with blood on their hands.

What America can do

The chances of a broad, tolerant, multi-sectarian coalition government emerging are not brilliant. The best organised of the Islamist parties in the United Iraqi Alliance is the Supreme Council for the Islamic Revolution in Iraq, better known as SCIRI. Some of its militias are sectarian, murderous and close to Iran. Too many of them are being incorporated whole, with their sectarian allegiances intact, in the new army and police. While Sunni suicide-bombers kill Shias in mosques and buses, SCIRI's friends assassinate and torture Sunnis. As the gulf widens, compromise becomes harder.

The new Shia ascendancy must realise that Iraq will become stable only if its new top dogs are

generous. If the Shias do not recognise this for themselves, America should use its influence as the new government's protector to squeeze some generosity from them. Otherwise the country will not hold together, and the blood of too many Iraqis—and too many Americans—will have been spilt in vain.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com OPINION

Intellectual property

The real lesson of BlackBerry

Dec 14th 2005
From The Economist print edition

Defending the patent system is more important than keeping BlackBerry up and running

EPA

NOTHING comes to the wronged so easily as righteous anger. After a vicious patent suit, the maker of the BlackBerry—the wireless e-mail gadget that chains the white-collar proletariat to its work—faces the threat of a court-ordered shutdown in America. The service's users (widely known as CrackBerry addicts) fret about coping without it; shareholders of Research in Motion (RIM), the Canadian company that makes the devices, are angry at their wilting share price; and the wider technology industry, from Silicon Valley to Shenzen, watches nervously, wondering what it means for anyone who uses intellectual property—ie, just about everybody.

RIM is generally regarded as the victim of an injustice. Founded 21 years ago by two engineering students who still help run it, the company is being held for ransom by a “patent troll”. The monster emerging from under the bridge is an entity called NTP, which doesn't actually make or sell anything—it doesn't even have a website, for goodness sake. But it has hired a handful of lawyers to enforce its patents and in settlement talks this week, it was demanding almost 6% of RIM's sales in America until 2012 when its patents expire—about $1 billion. NTP's threat of a legal injunction to shut down BlackBerry unless it pays up is viewed as little short of extortion.

The easy conclusion is that the patent system is being cynically used to wreck the livelihoods of honest folks who are the true innovators. That's wrong. The chief lesson of the BlackBerry saga is that patents are there to be protected. If the system is to have any meaning, its integrity must be upheld for the sake of the businesses that rely on it and the public that benefits from innovation.

For a start, RIM itself is the chief author if its own fate. In 2000, barely a year after the BlackBerry was introduced, NTP requested that RIM license its patents (which are based on the work of an inventor who earned around 50 patents over many years). In 2002 RIM suffered so devastating a legal defeat that it was ordered to pay NTP's legal bills. An appeals court largely upheld the

judgment against the company this year. During this time, BlackBerry users rocketed into the millions—yet at every turn, rather than license the patents, RIM resisted; and, as it has resisted, the bills have mounted.

Distressed BlackBerry users argue that too many of the world's workers rely on the device for the service to be shut down. But many of their jobs depend on the principle at stake in this case—that the courts should protect intellectual property because it rewards inventors by conferring a real title to an intangible asset. Business requires confidence that intellectual property will be respected and infringers brought to justice, regardless of whether the litigant is using the patent or not. Only with that security will firms patent and license their inventions, thus allowing others to use their ideas.

Fixed-line reforming

This is not to say the intellectual-property system is perfect. America's patent office is re-examining NTP's patents and has declared them invalid—not because they necessarily are, you understand, but for the baffling reason that when such disputes arise, the office wants the patent-holder to defend his title. Moreover, injunctions are not always appropriate in infringement cases—a matter that the Supreme Court has recently agreed to consider. So the system certainly needs reform, but it also needs defending.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

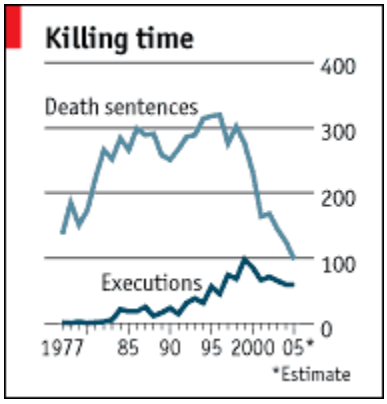
Economist.com OPINION

The death penalty

After Tookie

Dec 14th 2005
From The Economist print edition

The wrong decision in California, but America may be changing its mind



IN SOME contentious debates it is better to proclaim your prejudices at the beginning. *The Economist* opposes the death penalty: state-sponsored killing is inhuman, its effectiveness as a deterrent is at best unproven and it is no less prone to miscarriages of justice than more easily reversible sentences. We would not under any circumstances have wanted to execute Stanley “Tookie” Williams, who was killed by lethal injection in San Quentin this week (see article).

That said, it is possible to feel some sympathy for California's Republican governor, Arnold Schwarzenegger, who had to decide whether to grant clemency to the former gang leader. California's death row does not fit into the cartoonish version of American justice many foreigners have. The most populous state in the union has executed only a dozen out of the 1,003 people who have been killed since the death penalty was brought back in 1976 (Texas, by contrast, has executed 355). Although California has 648 people still on death row, it has had less than its share of the miscarriages of justice that have seen 122 American inmates now exonerated of the crimes for which they were originally sentenced to death.

Mr Williams, who helped start the Crips gang, was found guilty of four brutal murders in 1981. The evidence against him appeared conclusive and has survived various appeals. Mr Williams, however, always contested these convictions and therefore refused to apologise for them—an apparent lack of repentance that the governor thought counted against him.

Instead, Mr Williams's plea for clemency was based around what he did on death row. By the time he died, the gangster had acquired the air of a university academic. He wrote books urging young blacks not to join gangs and was nominated for two different Nobel prizes. Was Mr Williams's redemption genuine? Mr Schwarzenegger pointed to the fact that one of his books had been dedicated to a fellow inmate who died in a particularly bloody escape attempt. Others claimed the whole professorial act was a sham, whose purpose was merely to get him off death row.

Whichever way you look at it, Mr Williams presented a difficult decision for a Catholic governor trying to track back towards the political centre in a liberal state that supports the death penalty. Like a thoughtful Roman emperor, Mr Schwarzenegger let his thumb wobble before he turned it down.

It is, however, at precisely this point that revulsion at the whole circus of state-sanctioned killing begins to intrude. Was the result of Mr Schwarzenegger's thoughtfulness that much more “civilised” than Bill Clinton's famously barbaric race home to Arkansas during the 1992 campaign to sign the execution warrant of a mentally retarded man? The reasons the Gubernator cited are not watertight: if Mr Williams had admitted his crime, surely that would have pushed him towards

the chamber quicker? Above all, what purpose did his death serve, other than retribution? Mr Williams was surely doing more to prevent crime outside prison and encourage rehabilitation inside it while he lived. And there is also that tiny bit of doubt about his conviction.

Even when it is carefully administered, America's machinery of death still seems cruel and unusual. The United States is not the only democracy to retain the death penalty: Taiwan, Japan and India also do. But the number of executions it carries out puts it closer to China, Iran and Vietnam. Eighty-six countries, including all 25 members of the European Union (where murder rates are much lower than America), have abolished the practice altogether, and another 35 rarely use it.

Yet the row about Mr Williams also shows that America may be changing its mind. After steadily rising to a rate of 98 a year in 1999, the number of executions has fallen—to 59 last year and probably about the same this year, according to the Death Penalty Information Centre. Of the 38 states that retain the death penalty, 16 have not used it in the past two years. Public opinion has also been swayed by the publicity given to miscarriages of justice, especially in the light of DNA testing. Two years ago, Illinois's Republican governor commuted the sentences of 167 people on the state's death row.

Most Americans still support the death penalty, but the figure has fallen from 80% in 1994 to just 64% in a Gallup poll in October. The proportion falls further if the alternative is life imprisonment without parole, which is now an option in virtually all the death-penalty states. That has also helped the most encouraging trend of all: the number of death-penalty sentences has dived from around 300 a year a decade or so ago to fewer than 100 this year—the lowest level in three decades.

So America may be changing its mind. But that still leaves 3,400 people on death row. The next arrival in Emperor Schwarzenegger's Circus Maximus is a man whose 76th birthday is on January 16th, the day before his execution.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

London Stock Exchange

Clara's difficult Christmases

Dec 14th 2005
From The Economist print edition

Takeover bids do exchanges no harm: just look at the ones that are protected from them

RUNNING the London Stock Exchange is an eventful job. A year ago Clara Furse, the LSE's chief executive, was planning a big Christmas dinner at her country house when Deutsche Börse launched a takeover offer for the LSE. Amid high drama, Ms Furse saw off the German bid (and somehow served her guests as well). But, in spite of protests from the exchange's management that it would do best to stay independent, the LSE has faced near-constant speculation about an imminent takeover ever since.

This year, poor Ms Furse faces the prospect of yet another foreign bidder complicating her Christmas. As *The Economist* went to press, Macquarie Bank of Australia, which had made an initial, indicative offer for the LSE last week, looked likely to formalise a bid for the exchange (see article). Even if Macquarie decides to pull back at the last minute, other potential bidders are still waiting to pounce.

All this disruption has led to fears for the future of one of London's main financial institutions. The months of takeover speculation have proved distracting for the exchange's management, it is argued. Macquarie is a foreign, fast-growing investment firm with an unusual financial model that is known for buying toll roads, airports and real estate across the world, but it has no experience running exchanges. This worries some investors and has drawn scorn from the London exchange, which contends that the Australians have no good business case to offer. Reports that Macquarie has lined up a chunk of debt finance to pay for a prospective LSE bid are fuelling concerns that it may raise fees for exchange users if an offer is successful.

Fair enough, as far as it goes. But none of this proves that a bid for the LSE must be bad for the exchange and its customers. Exchanges are vital parts of the financial infrastructure of a centre like London, but shielding them from competition would be worse than exposing them to it.

Although detractors try to portray the circling bidders as a sign of weakness at the LSE, foreigners are drawn to the exchange chiefly because, in a world with many badly run exchanges, the LSE is a pretty good one—even though it could have a more coherent long-term strategy and should have grabbed a bigger share of the booming trade in derivatives. Along with New York, London sits head and shoulders above every other financial centre in the world. In this most global of industries, London attracts talent from everywhere. From the City, investment banks serve deep-pocketed customers across Europe and beyond. Companies from Russia to South Africa have chosen to list on the LSE, and its share-trading volume jumped 23% in the year to November. London's popularity among foreign companies is not just down to the LSE, but the exchange is a factor.

All the more reason, you might say, to fear the disruption a bid causes. But though prospective

offers are time-consuming, the threat of takeover is precisely what concentrates the minds of managers—especially in an age when exchanges are, like the LSE, no longer owned by their members.

Out of the frying-pan

Look at the mess in Japan this month for a glimpse of what can go wrong when managers' feet are removed from the fire. The reputation of the Tokyo Stock Exchange (TSE) was badly dented this week after its flawed share-trading system cost a big bank several billion yen by preventing the cancellation of a mistaken sell order (see article). The TSE, which suspended trading in all shares last month after another computer problem, lacks transparency, risk controls and technological sophistication. The exchange's shortcomings will, by extension, hurt corporate Japan.

The worries about higher user fees if the LSE changes hands look like a spot of gamesmanship on the part of investment banks. In the long run, raising fees will drive liquidity off the exchange. Big exchanges face threats from off-exchange trading and, in Europe, regulation coming into force by 2007 will blur the distinctions between over-the-counter and on-exchange trading. The LSE's own business plan sees its Alternative Investment Market luring mid-sized companies from continental Europe with the promise of low costs and deep liquidity. In other words, a strategy built around charging high fees hardly looks like a sensible one for the owner of the LSE—whoever that might be.

That leaves regulators with a minimal role—to ensure that any buyer has the capital and risk-management and audit systems it needs to run the LSE. In Britain that duty falls to the Financial Services Authority (FSA), which has in the past declared its indifference to the nationality of bidders.

Macquarie has no experience of running stock exchanges, but it uses exchanges across the world and should thus be attuned to investors' needs. The question of whether it—or any other bidder—is right to think it would do a better job than Ms Furse is (FSA permitting) a matter for its backers and the LSE's shareholders. Ms Furse's best course of action is clear: fight any bid on its merits and hire a good caterer.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

The pecking order

Runner-up, up and away

Dec 14th 2005
From The Economist print edition

Being second best is underrated

WHEN competition is fierce and elbows are flying, nothing is more natural than the desire to clamber atop the heap. The biggest firms in most industries have an edge. They probably became the biggest by being the best. They tend to become more efficient as they grow, reaping economies of scale, thus increasing their margins and their advantage over smaller rivals. Being large enough to shape an industry can help. And when the national champion is faltering, there is a fair chance politicians will consider it too big to fail.

So you might think that it's time to crack open a few cans of the fizzy stuff at PepsiCo, which this week surpassed Coca-Cola in market value for the first time in 112 years of frantic competition. And yet, without wishing to spoil Pepsi's party, the case for celebration is not so clear-cut. As America has discovered in the geopolitics business, being number one is not much fun.

As soon as a firm climbs above the sharp elbows of its rivals, it starts getting pelted with the eggs of anti-business activists. People who hate big business aim high. So while big, bad Wal-Mart is pilloried, Target has in the past couple of years blithely cut the benefits of its non-union workers. And when was the last time you saw an anti-globalisation mob destroy a Burger King outlet?

Unlike Microsoft, which is loathed by many for its monopoly power, Apple has not had to contend with thousands of young hackers vying to poke holes in the security of its operating systems. While Nike was inundated with complaints about its “sweat shops” in poor countries, Adidas steadily improved its brand, and has recently acquired Reebok to emerge as a strong number two. If only Ebenezer Scrooge had lived across town from a bigger rival, the ghosts of Christmas might have picked on the other guy, and left the poor curmudgeon to a good night's sleep.

As protesters get better at running media campaigns, the second-best advantage may even be growing. Firms such as Ford, Burger King and Target do not have documentary-makers queuing up to attack them in such films as “Roger and Me” (General Motors), “Super Size Me” (McDonald's) or “Wal-Mart: The High Cost of Low Price”. Even if the runner-up does get caught doing something unpopular, it can pin the blame on merciless competition from the evil number one.

Fairly big is beautiful

Second-biggest firms can also be easier to manage. The striving, inventive chasers at Pepsi spotted the current fashion for health faster than did complacent Coke (see article). Followers short of a strategy can point to the leader and tell everyone to give chase. They can often appeal to their customers by highlighting a leader's drawbacks. “We're number two, so we try harder”, the Avis car-rental agency used to say as a way to cash in on Hertz's smug service. When McDonald's was selling the same burger to billions, Burger King customised its meals and told customers to “Have it your way”. And big customers and suppliers, fond of having it their way, will often give the runner-up business to prevent a monopoly from emerging. Imagine a world in which Boeing or Airbus was the sole maker of commercial jets.

Spirits are probably low at Coke, but its people should console themselves. The big guys may get the numbers, but it's the runners-up that have all the fun.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

On Xinjiang, Italy, fat animals, the Balkans, pensions, snow, football

Dec 14th 2005
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

Minority report

SIR – Your article on China's strategic concerns in Xinjiang seriously understates the extent of human-rights violations in the region ("Under the thumb", December 3rd). Moreover, you gave the impression that government development policies have been more inclusive than in fact they are. By the Chinese authorities' own admission, Uighurs are not benefiting from such policies and on most indicators— longevity, education, health, income—are actually becoming worse off.

The government's response to staunch political opposition in Xinjiang has resulted in Uighurs being the only people in China executed for non-violent political "crimes". The crushing restrictions on religion, use of the Uighur language, and anything else perceived as "separatist", are prices that Uighurs are paying for Chinese "stability". The somewhat crass conclusion to your article, that Xinjiang is brutal but secure, is a surprisingly short-sighted observation. China is not preventing a security nightmare, it is creating one.

Nury Turkel
Uighur American Association
Washington, DC

Forza Italia?

SIR – Although your survey on Italy presented a fairly thorough analysis of the country, it was a little stereotypical in parts (November 26th). One example is your parallel with the situation in Argentina. Yes, Italy is facing all the problems of large continental European economies. However, after many years of "malaise", Italians now perceive that the party is over and are starting to act. Entrepreneurs are leading this movement and are relaunching their efforts to invest in international business and to press the government for more competition and reform. Luckily, there are not many people left in Italy who think they can prosper due to the favour of a good friend in politics. This is a good starting point at least.

Riccardo Monti
Director, Value Partners
Rome

SIR – It was surprising that you didn't mention the powerful labour unions, especially the CGIL, as a contributing factor to the crisis in Italy. While their popular support is declining, they can still command strikes that paralyse the country and can hold any government hostage, whether centre-right or centre-left. With a rhetoric, language and mind-set trapped in the ideology of the 1960s and 1970s, Italy's labour unions are the single most important adversary of economic and

labour-market reform.

Giorgio Cometto
Nairobi

SIR – The barons who run Italy's university fiefs are indeed the most overpaid and underworked teachers in the world. Language faculties, for instance, teach for two hours and 45 minutes per week for 30 weeks of the year. Their research is subsidised by the state and published in local corner shops, the open market being out of reach due to their pitiful quality. Thanks mainly to non-Italian lecturers, called *lettori*, who teach for 12 hours per week for a fraction of the pay, some students do learn something. The European Court of Justice, which has issued four previous judgments in favour of the *lettori*, recently heard Italy's lame-duck defence of its 18 years of job and wage discrimination against us based on nationality.

David Petrie
Association of Foreign Lecturers in Italy
Verona

SIR – You reinforced a long-held hunch of mine that Italy has much in common with Japan. Both countries have declining birth rates, live-at-home 30-year-olds, similar phonetic systems (formed by linking syllables based on the same five pure vowels), a long tradition of craftsmanship, a comparable geographic latitude, similar jingoistic ideologies (especially during the second world war), entrenched organised crime and bloated government bureaucracies. Moreover, both cultures eat squid and octopus.

Troy Fowler
Yokohama, Japan

Like a beached whale

SIR – Your article on obesity begins, “Wild animals are never fat” (“Bouncing back”, December 3rd) Have you ever looked at a walrus?

Charles Wells
Oberlin, Ohio

Balkan history

SIR – To consider Otto von Bismarck “a master of Balkan diplomacy” is to forget his considerable role in turning Macedonia into the first true terrorist state in history by handing it back to unconditional Ottoman rule at the Congress of Berlin (“Europe's *banlieue*”, November 26th). This blunder arguably galvanised the Young Turks into a rebellion that incited the Austro-Hungarians to annex Bosnia, the harsh treatment of which led to the spark of the first world war. With Macedonia still smarting over a century later, it can only be hoped that the disciples will humble the master.

Lucas Chambers
Lausanne, Switzerland

The work-life balance

SIR – The debate surrounding the Turner report on pensions in Britain is already degenerating into a squabble about input from the chancellor, Gordon Brown, instead of being used to confront people with the problem of their own retirement (“Britain's pensions pickle”, December 3rd). At

issue is whether we are all due a fully adequate pension from the state, or whether pension provision is essentially the responsibility of the individual. However, an adequate state pension is simply unaffordable, as the current experience of several European countries demonstrates. It would be a huge pity if debates about mortality tables and spending plans diverted attention from Turner's central arguments, which is that it is the responsibility of employees to retain their standard of living after retirement, even if the justifiable abandonment of final-salary schemes does not absolve employers from continuing to contribute.

Robert McFarland
London

Snow fake

SIR – I found your outlook on snowmaking at American ski resorts a little too peachy ("All-weather wonderland", November 26th). As someone who has skied for years at these resorts, I can assure you that regardless of where they aim the snow gun, Snomax, a "bacteria-derived protein", ends up all over you and tastes a bit as though you had turned an air duster upside down and shot it into your mouth. I, for one, would rather have patchy snow in the spring.

Ross Borden
Vail, Colorado

Calm down, calm down

SIR – Has the writer of your obituary on George Best lost his mind, or just his memory (December 3rd)? To suggest that only Arsenal and Chelsea can challenge Manchester United these days as an English footballing "superpower" is as ludicrous as it is inaccurate. Liverpool has won dozens of domestic and European trophies, including five European cups, a feat which no other British team has even come close to matching.

Mike Ormsby
Boston

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

American military tactics

How to do better

Dec 14th 2005 | FORT POLK AND MOSUL
From The Economist print edition

After brutal blunders in Iraq and Afghanistan, the American army has become more intelligent—and hopes to be more effective

Get article background

DOWN a rough track, glowing silver under the moon, rolls a black pick-up truck carrying a 500lb bomb. The white walls of the American army base loom, but no shout or shot comes. Your correspondent fingers his detonator.

Unchallenged, the truck drives alongside the base, then we blow ourselves up. The first blast, in a yellow flash, lights up a guard-tower and the anxious face of a young GI. The second, after we bombers have scrambled for safety, is much bigger—a hollow boom and an explosion of orange fire that soars 100 feet into the night sky, lighting up skinny pines all around. As the flames fall, *The Economist*'s fellow suicide-bomber shouts to the sentry: “Go tell your buddies, you're all dead.”

That should teach them not to leave open the approach to their perimeter, a mistake that cost many American lives in the early stages of Iraq's insurgency. But these soldiers will live. Their white walls are chipboard, the bomb is a “reduced-blast” special effect, and although fictionally in the Afghan region of “Talatha”, they are at Fort Polk in southern Louisiana, 200,000 acres of pine forest which the army uses for training. The soldiers, members of a 3,500-strong infantry brigade in the final stage of preparation for a mission to Afghanistan, will be extracted from the woods for 24 hours and then, chastened, reinserted to fight again.

Car bombs are not the only bit of Iraqi-Afghan verisimilitude the brigade experienced at Fort Polk's Joint Readiness Training Centre (JRTC) last month. Attacks with simulated roadside bombs (known as improvised explosive devices, or IEDs), rockets, mortars, rocket-propelled grenades (RPGs) and

small arms, using special effects and lasers, are unrelenting.

The assailants—160 American soldiers dedicated to the task, and dressed accordingly—come in two forms: al-Qaeda terrorists, based in an off-limits bit of the wood called Pakistan, and Taliban insurgents living in 18 mock villages. Another 800 role-players live with them, acting as western aid workers, journalists, peacekeepers, Afghan mayors, mullahs, policemen, doctors and opium farmers, all with fake names, histories and characters. Some 200 bored-looking Afghan-Americans are augmented by local Louisianans in Afghan garb. A clutch of Vietnam-veterans with missing limbs, splashed with fake blood, make terrific bomb victims.

Fort Polk has seen huge changes in the past two years. Designed for light infantry and special-forces troops, it has always dealt with some parts of guerrilla warfare, such as booby-traps and RPG attacks. But in the past the “insurgents” wore blue armbands to distinguish themselves, a tactic strangely shunned by America's enemies in Iraq and Afghanistan. There also used to be no more than 50 civilian role-players on the battlefield.

The changes are expensive—the basic cost per brigade of a month at the JRTC has gone up from $2m to $9m. And similar changes are under way at the army's two other Combat Training Centres (CTCs), where the army simulates battalion- and brigade-sized battles. Fort Irwin, California, used to be dedicated to tank battles. Two years ago, not a single building dotted its 600,000 acres of desert. Now there are a dozen mock villages and plans for a $50m mock city. Two Hollywood companies have been hired to improve the army's flashes and bangs, and to give acting classes to the role-players.

A catalogue of blunders

Stung by its setbacks in Iraq and Afghanistan, the American army is trying to change. The challenge is immense, and the army's recent past suggests reasons for cynicism.

Since quitting Vietnam in 1973, America has fought dozens of counter-insurgencies and small wars. But most of those, in Central America, were mainly special-forces operations. And in places like Somalia and Haiti it often made the same blunders as against the Viet Cong. If the army's rules of engagement were stricter, there were still too many strikes on innocent targets, too much use of firepower and too little effort to understand the culture. Faced with a counter-insurgency, the American army's preferred tactic was attrition.

Of course, all wars are different. No previous campaign could have provided a blueprint for success in Iraq. Suicide-bombers are a different threat from Marxist guerrillas. But history can suggest a few solid principles for successful campaigns against insurgents; and too often, in Iraq, American troops have ignored them. A pre-Iraq comparison between the American and the British armies is instructive.

In their routine planning and training, the British expected to find civilians on their battlefield; the Americans did not. The British taught the virtue of restraint, to limit civilian casualties and the strategic damage they cause. American soldiers were trained to wipe the enemy out. British soldiers were trained in crowd control and basic forensic skills; American soldiers rarely were. In April 2003, nervous American soldiers fired into a crowd of protesters in Fallujah, killing and maiming scores. Within weeks, the Iraqi town had risen against the occupation, culminating in two terrible battles last year.

In more peaceable southern Iraq, meanwhile, the British acted on their training. Their first aim was to win the civilian population's trust. One way was through information operations (IO), which means, at the crudest level, generating good public relations for the army. “The Brits do this as a

matter of course; they had a much finer appreciation of the culture in Iraq," says Lieutenant-Colonel Chuck Eassa, deputy-chief of IO at Fort Leavenworth in Kansas, the home of the army staff college and other cerebral institutions. For the American army in Iraq, he says, IO was a "low-density skill set". Each division of 19,000 soldiers had only two IO officers.

Another way to win trust is the British habit of doffing helmets and patrolling on foot. This is not always possible: when a Shia insurgency flared in southern Iraq last year, the British hunkered down behind armour and killed wave upon wave of fanatics. But when the violence ebbed, they had the flexibility to revert to friendlier tactics. To see a British sergeant in southern Iraq dismount from a Land Rover fully kitted for war, assess the local mood, then call, "Right lads, hard hats off," is impressive. According to Lieutenant-General Sir John Kiszely, formerly deputy-chief of coalition forces in Iraq and now head of the British Defence Academy: "In future, probably nine out of ten operations will not be purely war-fighting. The soldier of the future will have to be a warrior—but much more as well."

Giving grief, Iraqi style

In part, the American army's unreadiness for dealing with civilians stemmed from a reliance on signal, not human, intelligence. As a battle raged in Iraq's northern capital of Mosul last year, shortly after its police force had collapsed, an American lieutenant-colonel showed this correspondent his control room. On a cluster of computer screens, he could see, in real-time, where each of his Stryker armoured vehicles was and what it was seeing. "It's like Sun Tzu said," he enthused, recalling an ancient Chinese military strategist, "to win a war you need three things: to see the battlefield, to see yourself...so now I guess I just need to see the enemy." If the enemy is hidden among the general population, technology can help, but it will not complete the task.

In a recent comparison of the British and American approaches, "Counter-insurgency lessons from Malaya and Vietnam," John Nagl, a retired American marine officer, argues that Britain's relative expertise was not merely the result of its imperial history. In Vietnam, after all, America had ample experience of acting as an occupying power. Moreover, in both Malaya and Northern Ireland, the British were at first heavy-handed and unsuccessful. The difference, says Mr Nagl, is that the small British army was able to learn from its mistakes and change, while the bigger American army was not. Can it really be doing any better in Afghanistan and Iraq?

Tips from the ground

The signs are mixed, but encouraging. Take, for instance, the way the army is involving all its soldiers in setting TTPs—the tactics, techniques and procedures that define how it acts on the battlefield. The idea is that every TTP—be it the appearance of a new sort of bomb in Baghdad or a new way to disable one—holds lessons for army doctrine, training, appropriations, research and development and so forth.

Every brigade in Iraq and Afghanistan now has a secure intranet page, which soldiers are encouraged to fill with observations and queries. Early this year a secure online chat-room, the Battle Command Knowledge System, appeared. Besides circulating thousands of tactical questions and answers, it can help soldiers find technical experts, learn foreign languages, contact counterparts in the war zone, or squint through the web camera of an armoured vehicle in Iraq.

At Fort Leavenworth, the rather wonderfully named Centre for Army Lessons Learned (CALL) has catalogued 6,200 battlefield and training-ground observations in the past four years and produced 400 reports on them. Its staff has tripled. “They've been pumped full of steroids,” says Lieutenant-General David Petraeus, Fort Leavenworth's commander, who has recently returned from Iraq.

Cynics spot some familiar aspects to all this. Although the Pentagon is spending a fortune on bureaucratic processes, some think it remains weak on analysis and incapable of self-criticism. “Lessons Learned” is, after all, not the same as lessons learned—as CALL's boss, Colonel Larry Saul, admits. Mr Saul says a key lesson from Iraq and Afghanistan is that American soldiers must know a smattering of the local language. When assured that almost no American soldier knows six words of Arabic, Dari or Pushtu, he admits: “I can take a horse to water but I can't make him drink.”

The evidence is indeed mixed, but there are many signs of progress, even in Iraq. The American army has trained more than 100 Iraqi battalions in little over a year; fighting alongside them, it has come to understand their culture better. It is also more restrained; atrocities like the killing in Fallujah would be less likely now.

In an example recently praised by George Bush, the 3rd Armoured Cavalry Regiment carried out a model attack on insurgents in the northern Iraqi town of Tal Afar in September, first emptying it of civilians, then giving Iraqi soldiers the lead in the offensive. This success was, in large part, a response to failure, according to the regiment's commander, Colonel H.R. McMaster. On a previous deployment to Iraq, in western Anbar province, the unit had done terrible damage with random and aggressive house-to-house searches, mass arrests and thuggish crowd control. Since arriving in Tal Afar last April it had patrolled often and on foot, looking for human intelligence, and had avoided making indiscriminate arrests.

But Colonel McMaster was relatively lucky. He had seasoned troops, and enough of them, to control his area. The marine division currently in Anbar, Iraq's most violent province, is too thinly spread and too shot-at to develop such nice behaviour. Unable to get control of the rebellious towns in the Euphrates river valley, often supported by air strikes but rarely by Iraqi troops, the marines are fighting a mid-intensity war.

There are other impediments to the army's improving counter-insurgency skills. One is the dismal record of many civilian agencies in Iraq. Some $20 billion has been spent on restoring Iraq's basic services, but with little noticeable improvement—hardly the way to win hearts and minds. Another snag is the army's fixation with self-protection. In Mosul, your correspondent strolled through a souk with a dynamic and thoughtful American captain who chatted and waved to the shoppers, trying to win trust. But with his face hidden behind helmet, headset and mirrored-shades, women and children saw him and fled.

Changing an army's approach takes time. The warrior spirit, as Americans call their propensity for macho soldiering, or killing people, is deep in their military culture. In Afghanistan's violent Helmand province, an American special-forces captain—with broad experience of counter-insurgency—analysed his furtive Taliban enemies thus: “They're cowards. Why don't they step up and fight like men?” Apparently, he had not considered how he might fight if he had no armour, no radio, an ancient rifle and the sure knowledge that if he fought like a man, he would be obliterated in minutes.

Revising doctrine

Off the battlefield, the army's lesson-learning is easier to measure. At Fort Leavenworth, big changes have been made. The 1976 edition of “Operations”, the standard manual of best practice

in warfare, did not mention counter-insurgency, and the army's dedicated counter-insurgency doctrine manual was last rewritten in 1965. But the section of the current edition of “Operations” dealing with counter-insurgency is now being revised, and a new version of the counter-insurgency manual, written with British help, was distributed as an interim draft on October 1st.

Next time, it's real

According to the new doctrine's authors, at Leavenworth's Combined Arms Doctrine Directorate, key changes will stress the strategic importance of civilian populations. The army's basic doctrinal aim is to move from high-intensity offensive to low-intensity security and stability operations—from creating shock and awe to winning hearts and minds. The new doctrine will emphasise that, where possible, the two levels should co-exist—where possible, for example, the army should exercise restraint in its offensive operations. In addition, the revised “Operations” will stress the need to protect civilians from external threats (such as Islamic terrorists) and internal disorder (such as looters), while ensuring the provision of “central services”, including power and water.

The interim counter-insurgency manual also reflects recent failings. It suggests ways to stop a conventional war turning into an insurgency. One way is to avoid upsetting civilians, among whom insurgents can hide, by being more sensitive to ethnic, tribal and religious differences.

Other corners of Fort Leavenworth bustle with change. A “Red University” has been established to teach “red teaming”, or second-guessing enemies and allies; it will accept its first students in January. A “red team”, dedicated to predicting future threats and to replicating them in training, has been doubled since 2002. Courses in IO have been increased from two to ten weeks. At the army staff college and a more select school for army planners, the School for Advanced Military Studies, the biggest change is that 45% of the students have recent combat experience. This fully professional army is much likelier to remember its lessons than the conscript army that withdrew from Vietnam.

But it is at the CTCs, including that bomb-blasted patch of Louisiana pine woods, that the army's effort to change its ways is most visible. Two years ago, with few civilian role-players on the mock battlefield, the soldiers' main objective was to bypass them and kill the enemy. Now most training involves civilian role-players. Even when launching an attack, the soldiers must bear in mind the overarching need for stability.

According to Brigadier-General Michael Barbero, Fort Polk's commander, “We're working hard at instilling shades of grey, at teaching commanders not to just kick in doors, to get among the

population and gather intelligence." This change, incidentally, makes the CTCs extremely similar to the British army's Operational Training Advisory Group, which has used role-playing for two decades. The biggest difference is money. American soldiers at the CTCs are shot with lasers and Hollywood-quality special effects; in mock battles at Tin City, a fake town in the Kentish countryside, unlucky British soldiers are ignited with petrol bombs.

A favourite buzz-phrase at Fort Polk is "consequence management", or weighing the goal of an operation against its other results. During daily meetings, the training officers discuss, often in staggering detail, the brigade's latest actions, and plan their reactions accordingly. Thus, for example, a company commander has failed to deliver medicines to a village clinic, run by a "Dr Jihad", as promised. In response, a "journalist" is commissioned to report the story for the *Talatha Times*. This prompts al-Qaeda fighters to deliver medical supplies to the clinic, and, in the process, they forge ties with the local Taliban. The two groups collaborate in a fierce attack on the offending American company, using car bombs, IEDs and indirect and direct fire, killing and wounding dozens. That will teach them to keep their promises.

It is unclear how long the CTCs will keep their lavish resources. Since early 2003, every training rotation has been geared to preparing a brigade or battalion for a mission in Iraq or Afghanistan. As America withdraws its troops from Iraq—whenever that will be—non-mission-specific training will resume, and the training budget will be cut. But Brigadier-General Barbero says he hopes to retain enough cash for a decent number of role-players on his mock battlefield. And he expects, culturally, that they will remain Islamic.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

A new front in the culture wars

The Lord's word

Dec 14th 2005 | LOS ANGELES
From The Economist print edition

Are secular universities discriminating against religious schools? Or are they just setting high standards?

Get article background

IN ITS opening pages, “Biology for Christian Schools” (Bob Jones University Press) comes straight to the point:

> “The people who have prepared this book have tried consistently to put the Word of God first and science second. To the best of the author's knowledge, the conclusions drawn from observable facts that are presented in this book agree with the Scriptures. If a mistake has been made (which is probable since this book was prepared by humans) and at any point God's Word is not put first, the author apologises.”

And that is precisely why a high-school science course using the 693-page book as a primary text does not meet the admission standards of the University of California (UC). It does not, argues the university, reflect “knowledge generally accepted in the scientific and educational communities and with which a student at the university level should be conversant.” The same, says the university, is true of some other courses—in history, literature and government—offered by Calvary Chapel Christian Schools of Murrieta, a small town south-east of Los Angeles. These courses also rely on books from the Bob Jones University Press and from another Christian publisher, A Beka Books.

Welcome to the latest front in America's culture wars. The Association of Christian Schools International (ACSI), the Calvary Chapel Schools and six Calvary Chapel students are suing the university, whose campuses include that traditional bastion of liberal thought, Berkeley, as well as the huge UCLA campus, for what they call “viewpoint discrimination”. The Christian schools add

that the university is violating the students' constitutional right to freedom of speech and religion. The university naturally denies the charges, and this week a federal judge in Los Angeles began considering the preliminary arguments of a contest which could eventually reach the Supreme Court.

So far the UC case has had less publicity than the argument about whether high schools can teach “intelligent design” as an alternative to evolution (currently being fought out in a courtroom in Pennsylvania) or even a ferocious dispute up in Cupertino, where a history teacher claims he was restrained from teaching about Christianity's role in American history (parents had complained that he was acting more like an evangelical preacher). In fact, all these arguments are part of the same battleground, which pits an increasingly self-confident evangelical America against a secular education establishment.

The ACSI, which represents almost 4,000 Christian high schools in America, including some 800 in California, worries that if the Christians' challenge fails, UC's intolerance might spread to other institutions and other states. Moreover, says a lawyer for the plaintiffs, victory would be “a major blow to the arrogance of the ivory towers and their attempt to say that kids from Christian schools can't be well prepared for university.”

There is a lot at stake. California, with its ten-campus UC system and the 23-campus California State network, has America's biggest—and best—system of public universities. The case has arisen because of the way that UC, unlike other systems, intrudes into high-school education. Its Board of Admissions and Relations with Schools assesses high-school courses to see if they meet its standards (known as “A-G requirements”, and ranging from a two-year history syllabus to one-year elective courses in subjects such as the visual and performing arts).

UC denies it practices secular intolerance and “viewpoint discrimination”. It notes that it has approved plenty of courses at Christian schools and in the past four years has accepted 24 of the 32 applicants from the Murrieta school. And it says that if the courses had used these textbooks “as supplementary, rather than primary, texts, it is likely they would have been approved.”

What is really being challenged, says the university, is its right to set its own academic standards and admission requirements. In which case the question is what that right implies. The Christian plaintiffs say they have no objection to science students, for example, being taught conventional wisdom, but “their constitutional rights are abridged or discriminated against when they are told that the current interpretation of scientific method must be taught dogmatically, and must be accepted by students, to be eligible for admission to University of California institutions.” In other words, what the case involves is not so much the now-familiar tussle over intelligent design, but a student's freedom of speech and thought.

All of which, counters the university, is bogus. As long as they satisfy the A-G requirements, students who are headed into the UC system can believe whatever they choose to and take whatever additional courses—including religious ones—they like. In any case, the university's lawyers point out, there is plenty of precedent establishing a university's right to control a student's speech: witness a court ruling three years ago that a UC student did not have a first amendment right to write “fuck you” to university administrators in his master's thesis.

In theory, the UC case stops at California's borders: no other state's public universities interfere so much in the high-school system, so their “secular intolerance”, real or imagined, is less potent. In practice, whatever happens in the current case, more such conflicts will follow.

For instance, when home-schooled children or students from private Christian schools apply to a public university, they are typically judged by their examination scores—and, typically, they are required to perform much better than their counterparts from the public schools. By the reckoning

of the Calvary Chapel plaintiffs, a student from a Christian school in California needs to score within the top 2-4%, whereas a public-school teenager with good course-work could meet the required score almost by guesswork.

Given the growth across America in both home-schooling and Christian schooling, there will surely be more “viewpoint-discriminated” students and their parents contacting their lawyers. And evangelical America will keep pushing. Christian universities such as Wheaton, in Illinois, are proof that decent scholarship can co-exist with evangelical faith; and, given the rise of born-again Christianity across the nation, more evangelical scholars are now found in secular faculties.

Fifty years ago there were only a handful of “megachurches”, drawing more than 2,000 each Sunday; today, there are more than 1,200 such churches, three of them with congregations of over 20,000. Not only is the nation's president a born-again Christian, but so (according to the Pew Research Centre) are 54% of America's Protestants, who are 30% of the population.

Will America's public universities take on a similar tinge? To the extent that educational establishments reflect cultural reality, it may be inevitable. After all, before the liberal era of the 1960s, there were no such things as courses in “Women's Studies” or “African-American Studies”. Now, no prudent American university would be without them. It would be odd if conservative Christians did not leave similar footprints on the syllabus.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

The death penalty

Tookie v Arnold

Dec 14th 2005 | LOS ANGELES
From The Economist print edition

A tussle where one man died, but neither won

IN THE end, Arnold Schwarzenegger was unmoved by the pleas of his Hollywood friends, of the Rev Jesse Jackson, of Snoop Dogg, of Bianca Jagger and all the other luminaries begging him to spare the life of Stanley "Tookie" Williams, the 51-year-old co-founder of the Los Angeles street-gang known as the Crips. "Is Williams's redemption complete and sincere," mused California's governor, "or is it just a hollow promise?"

Answering his own question, Mr Schwarzenegger argued that there could be no possibility of clemency unless Mr Williams were first to apologise for the murder of four people in two separate armed robberies in February and March 1979. But throughout his 24 years on death row in San Quentin prison, Mr Williams maintained his innocence, basing his claim for mercy on his renunciation of the gangs and a series of books warning children against the life he had led.

For Mr Schwarzenegger, that was not enough: "In this case," wrote the governor in his decision on December 12th to deny clemency, "the one thing that would be the clearest indication of complete remorse and full redemption is the one thing Williams will not do." Accordingly, Mr Williams died by lethal injection in the early hours of December 13th.

The decision to kill Mr Williams was the most angst-ridden for any California governor since Ronald Reagan spared a mentally deficient murderer some 38 years ago. Mr Schwarzenegger was particularly swayed by the fact that Mr Williams chose to name George Jackson among the dedications of his book, "Life in Prison". Jackson died in a violent attempt to get out of San Quentin in 1971 after a riot left three officers and three inmates dead. The inclusion of Jackson, argued the governor, showed that Mr Williams "still sees violence and lawlessness as a legitimate means to address societal problems".

Refusing clemency was, in political terms, a safer choice than granting it. Nationwide, the number of people being sent to death row has fallen sharply, as doubts have risen about its efficacy and juries have opted to send people to jail without parole; the number of executions is also down (see chart above). But most Californians support the death penalty (54% of Democrats and 87% of Republicans, according to a Field poll last year). Significantly, neither Phil Angelides nor Steve Westly, the two Democrats who have declared their intention to run against Mr Schwarzenegger in next year's election, opposes the death penalty.

One reason for public support may be that California's executions—thanks to a careful appeals system—are so rare. Mr Williams is only the 12th person to be executed in the state since the

Supreme Court re-instated the death penalty in 1976. By contrast, Texas has executed 355. California does not yet have its equivalent of Ruben Cantu—a San Antonio man who was executed in 1993 for a shooting that the *Houston Chronicle* seems to have now proved he almost certainly did not commit.

AP

How he arrived. How he left.

Mr Schwarzenegger is still trying to gain his political footing. It is barely a month since the electorate convincingly rejected four ballot initiatives sponsored by the governor in a special election widely regarded as expensive and unnecessary. That result convinced the governor that he had veered too far to the right—and had better reclaim the centre ground that got him elected in the first place.

Mr Schwarzenegger's immediate answer has been to hire as a new chief-of-staff Susan Kennedy, an openly lesbian, Democratic, abortion-rights activist who was a chief aide to the Gubernator's Democratic predecessor, Gray Davis. For many of the Republican faithful, Ms Kennedy's appointment was a provocation, barely softened by a subsequent shuffle that shunted Terry Tamminen, a liberal Democrat, from his post as cabinet secretary and replaced him with Fred Aguiar, a conservative Republican. In their fury, conservatives are even talking of drafting Mel Gibson as a Republican opponent to the governor in next June's primary. That may be so much posturing—but imagine how much angrier the right would be if Tookie Williams were still alive.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Richard Pryor

Rebel with a cause

Dec 14th 2005 | ST LOUIS
From The Economist print edition

He changed racial comedy with one word in particular

AP

He played from Peoria

ONE lasting relic from the Watergate scandal is a catchphrase. “Will it play in Peoria?”, wondered John Erlichman, as he discussed one of Richard Nixon's schemes. The otherwise blameless Illinois city became synonymous with middle America—conventional, boring and safe.

Richard Pryor, who died last week, was none of those. The son of a Peoria madam, Mr Pryor began his career in dives, but built a career as a kind of younger Bill Cosby, gently poking fun at life from a black perspective. One night in Las Vegas in 1967 he looked at his audience and asked himself out loud what he was doing there. He walked off stage and dropped out of sight.

The Richard Pryor who reappeared in the 1970s was no sage Negro. He was an angry black man who broke the “N-word” taboo, turning the term of hate for blacks back upon the world. It was vicious, honest and very funny. It also ironically helped him “cross over” to white audiences. He was paid more money to appear in one Superman film than the star, Christopher Reeve. With Gene Wilder, he also created the inter-racial buddy genre in films like “Silver Streak” and “Stir Crazy”.

Mr Pryor's live act reflected the pain of his own life, his multiple marriages, his rough background, his drug use and drinking that almost killed him. He set himself on fire freebasing cocaine and heard that he had died on television in the hospital. He made a painful recovery, a story retold in “Live on the Sunset Strip”. But multiple sclerosis took away most of the past 20 years.

Even though he could no longer perform on stage, Mr Pryor's work lived on in a new generation of comics like Eddie Murphy, Chris Rock and Dave Chappelle who learned their craft listening to his records. Mr Pryor claimed that on a trip to Africa he realised the ugliness of the word “nigger” and renounced it, but the Pandora's box he opened with the N-word is still open. One of his characters, Mudbone, a world-weary blues musician, said there were only two things you had to do in this world: stay black and die. Mr Pryor did much more.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

The Patriot Act

Of liberty and libraries

Dec 14th 2005 | WASHINGTON DC
From The Economist print edition

The administration struggles to keep all its powers to catch terrorists

Get article background

"BEFORE the Patriot Act, it was easier to track the phone calls of a drug dealer than the phone calls of a terrorist. Before the Patriot Act, it was easier to get the credit card receipts of a tax cheat than those of an al-Qaeda bankroller."

And that, said George Bush in his weekly radio address, is why Congress should renew the USA Patriot Act, key provisions of which will expire at the end of this month. The law, passed after the attacks of September 11th 2001, has been used, he said, to "break up terror cells in New York, Oregon, Virginia, California, Texas and Ohio". If Congress fails to renew it by December 31st, he warned, Americans would lose "valuable protections", "but the terrorist threats will not expire on that schedule."

As *The Economist* went to press, however, it was unclear whether the act would be reauthorised. Several senators charged that it gives investigators too much power to snoop on the innocent. Senator Russ Feingold of Wisconsin, the only senator to oppose the original bill, threatened to filibuster it—to prevent a vote by waffling indefinitely on the Senate floor. And this time he will not be the only naysayer.

The act's most controversial provisions concern "roving wiretaps", "sneak-and-peek" warrants and libraries. A roving wiretap is when investigators are permitted to eavesdrop on any calls made by a terror suspect. In the days before cellphones and BlackBerries, warrants were typically granted only for a specific telephone. Police deem this out-dated, as a suspect can switch rapidly from one cellphone to another. Roving wiretaps have proven useful in snaring drug dealers. The Patriot Act gives even greater latitude in using them against terror suspects.

Sneak-and-peek warrants allow investigators to enter and search a suspect's house without informing him for several weeks. Before the Patriot Act, this power was used to nab mobsters. In one case, the FBI entered the house of Nicky Scarfo junior, a mafioso, and placed a "keystroke logger" on his computer, which enabled them to discover the passwords he used to protect his illegal-gambling records. Had they been obliged to alert Mr Scarfo to what they were doing, this obviously would not have worked. Under the Patriot Act, the same powers have been used to uncover bank accounts used by suspected sponsors of terror and to freeze them before the money could be moved.

"Libraries" is shorthand for the fact that the Patriot Act allows investigators to demand all kinds of records: which books a suspect has borrowed from a library, his credit-card records, his business accounts, and so on.

The Patriot Act's defenders argue that it is common sense to give the same tools to those pursuing terrorists as are given to those pursuing lesser criminals. It helps to know if a suspect has

borrowed a bomb-making manual, and the public's interest in preventing terrorists from making bombs outweighs any concerns that the FBI might discover embarrassing facts about innocent people's reading habits.

“It would be absurd to create safe havens [for terrorists] in libraries,” says Frank Gaffney of the conservative Centre for Security Policy. He argues that the Patriot Act has allowed an important change of tactics, from trying to prosecute terrorists after they strike, to gathering reams of useful information before they do. In this way, he reckons, it has “contributed to the fact that we have not been attacked again”.

Civil libertarians disagree, arguing that the act gives the authorities too much power to collect information about people who may have no connection to terror. The *Washington Post* reckons that each year 30,000 “national security letters” (demands for information under the act) are sent to businesses, libraries, hospitals and so forth. The administration insists that such letters are subject to adequate judicial oversight. But Senator John Sununu, a Republican from New Hampshire, complains that not one has been rejected.

The American Civil Liberties Union (ACLU) suspects that investigators are going on “fishing expeditions”—carrying out broad searches on flimsy grounds, in violation of the constitution. But it is hard to tell, since those who receive national security letters are barred from talking about them.

Concrete examples of abuse of the act are difficult to pin down. James Carafano of the Heritage Foundation, a conservative think tank, says this is because they are rare. The ACLU, however, cites the case of Brandon Mayfield, a Muslim American wrongly suspected of involvement in the Madrid train bombing of 2004, whose home was searched and who was held for a couple of weeks as a “material witness”. He was released, but his computer files and DNA samples were not returned to him, says Lisa Graves, the ACLU's senior counsel for legislative strategies. Without the Patriot Act, she says, Mr Mayfield would not have been so abused.

Republicans in the Senate and House last week proposed some tweaks to the Patriot Act to address civil-libertarian concerns. Under these, federal agents must obtain a court review before accessing library records, people who receive national security letters may consult with a lawyer, and those subjected to “sneak and peak” warrants must be informed within 30 days. This compromise was not enough to attract any support from Democrats, however. Patrick Leahy, the senior Democrat on the Senate Judiciary Committee, called for the Patriot Act to be extended for a mere 90 days, so that further safeguards could be agreed. The White House is pressing for a vote this week.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD NORTH AMERICA

Litigation and health care

Scalpel, scissors, lawyer

Dec 14th 2005 | ROCKVILLE, MARYLAND
From The Economist print edition

Health-care litigation costs America far too much

AS ANYONE thinking of having a baby in Maryland will know, it's not easy to find an obstetrician in the Old Line State. The main reason, says Debbie Redd, the head of Capital Women's Care (CWC), the largest group of obstetrician/gynaecologists in the Washington, DC, area, is that it costs $118,000 a year to insure just one of them against malpractice lawsuits. That is more than the total cost of employing a doctor in most countries.

Trial lawyers argue that malpractice lawsuits deter negligence. Craig Dickman, an obstetrician affiliated to CWC, says they mostly deter the kind of behaviour that might get you sued, which is not the same thing. To cover himself, he says, he orders excessive tests, monitoring and consultations with specialists. He guesses that 12%-15% of the procedures he bills for are unnecessary. If he fails to order every imaginable test, even if there is “no clinical evidence of efficacy”, he is exposed if something were to go wrong. A trial lawyer can scour the country for the one expert who thinks that his omission might have caused the patient's injury.

Dr Dickman has been sued five times in 21 years on what he (inevitably) describes as specious grounds. That is not unusual for an American obstetrician: 76% of them have been sued at least once. (They are more at risk than most doctors, since they typically operate on healthy patients, who may then blame them if they become ill.)

When doctors win cases, as they usually do, they still lose, because they have to pay their legal bills. And when they lose, they lose big. In jury trials, the average award of damages against a doctor is $4.7m. How much they have to pay to insure against these costs depends on where they practice. In St Clair County, Illinois, neurosurgeons paid an average premium of $228,396 in 2004, five times more than their colleagues in Wisconsin did. Inevitably, doctors (and insurers) flee the states that are friendliest to plaintiffs. Pennsylvania lost a third of its general surgeons between 1995 and 2002.

The cost of medical-malpractice lawsuits has risen more than 2,000% since 1975, to $26.5 billion in 2003, according to Tillinghast, an actuarial consultancy. And to what end? A study of malpractice suits in New York by the Harvard Medical Practice Group found that plaintiffs had actually been injured by doctors' negligence in only 17% of cases. Those patients with small claims often cannot find a lawyer to represent them, while those who win find their lawyers have swallowed half the payout from the doctors.

American health care is bedevilled by two problems that lawsuits do nothing to heal. First, health care costs too much. Americans pay twice as much per head for health care as people in other rich countries. Rising health-care costs threaten the solvency not just of private firms such as General Motors but ultimately also of the government itself. Second, some 46m Americans languish uninsured.

The problems of an industry that chews up 15% of GDP ($1.6 trillion in 2003) plainly cannot all be

laid at the lawyers' door. But they do help push up prices (and thus increase the number of uninsured). For instance, in the 1990s, health-maintenance organisations cut costs by trying to cover only treatments that were proven to work. But patients who were denied experimental treatments, and the hospitals that wanted to be paid for providing them, started to sue. After being slapped with a few multi-million dollar verdicts, HMOs more or less gave up trying to ration treatment and just raised their premiums instead. The cost of covering a family soared 59% in the four years from 2000, and the proportion of small firms offering employees health insurance fell from 68% to 63%.

A cure indeed

Can legal costs be curbed? You might imagine that the Democrats would be keen to change a system that leaves so many poor people uninsured, overcharged and uncompensated. But the party gets a lot of money from trial lawyers and even chose one, John Edwards, as its vice-presidential candidate last year. So it is left to the Republicans (who get even more money from insurers and hospitals) to be the keenest promoters of tort reform.

Earlier this year, Congress passed a bill forcing most big class-action suits to go through the federal courts, thus preventing lawyers from shopping around for the most plaintiff-friendly local courts. That may help drug firms, who complain that awards for faulty products are out of all proportion to the damage; and that the costs deter research by lowering the expected returns to it. Wyeth, a drug firm, has set aside $21 billion to settle lawsuits over Fen-Phen, a diet drug, while Merck, another drug firm, is expected to have to pay between $18 billion and $50 billion for having released a painkiller called Vioxx.

Both drugs were faulty—tests suggested that they caused heart problems in some patients. So the scope of the eventual settlements will give some clue as to whether the legal bandwagon has slowed down. Drug firms are not wildly optimistic that it has. Although the first federal prosecution against Merck collapsed this week, it is still facing 6,500 suits related to Vioxx, and was ordered by a jury in Texas to pay $253m to the family of just one victim.

Such awards are usually reduced on appeal, but the industry's chief complaint is that juries are unable to distinguish between good and bad science. Safe products, such as Norplant, a contraceptive device, have been hounded off the American market. Drug firms are especially reluctant to develop pills for people who are well, which is why no American drug firm has produced a new contraceptive since Norplant was withdrawn in 2002.

Class-action suits matter less to individual doctors and hospitals. The Republicans have made less progress when it comes to reforming straightforward medical malpractice. That is partly because most Americans want to be able to sue their doctor. But it is also because many of the costs of the current system are hidden. Studies have found that “defensive medicine”, of the sort Dr Dickman describes, more than doubles the costs that malpractice suits impose on health care, and sometimes prompts doctors to hack patients around more than is healthy.

For example, few clinicians think that babies get cerebral palsy because the obstetrician failed to deliver them by caesarean section. But smooth lawyers like Mr Edwards have made a fortune by convincing juries that this is the case. The fear of being sued prompts doctors to perform unnecessary C-sections—a risky and invasive procedure. But a five-fold increase in C-sections in rich countries in the past three decades has brought no decrease in the incidence of cerebral palsy.

James Copland of the Centre for Legal Policy at the conservative Manhattan Institute, author of a recent study called “Trial Lawyers Inc”, estimates that the total costs, direct and indirect, of

health-care litigation (including suits against doctors, drug firms, HMOs, nursing homes and so on) could be as much as $200 billion—a Hurricane Katrina every year. This figure involves some heroic extrapolation, but even half that sum would seem a lot to pay for a system that is not even good at compensating patients who are injured.

So what can be done? Some “solutions” look bizarre. Maryland's state government, for example, pays a portion of doctors' insurance bills, thereby adding to the pot that lawyers feed on. (A 10th-century English king, Aethelred the Unready, tried something similar when he offered bloodthirsty invaders cash or “Danegeld” to go away; oddly, they kept coming back.)

A more sensible idea would be specialist medical courts, as proposed by Philip Howard of Common Good, a group that lobbies for legal reform. Cases could be decided by judges who heard only medical cases, rather than by juries. The court could call its own neutral expert witnesses, rather than relying solely on the partisans hired by the litigants. Non-economic compensation for pain and suffering would be according to a fixed schedule—so much for an arm, etc—rather than by having jurors pluck a number out of the air.

The idea is partly modelled on the specialist courts that deal with other complex technical issues, such as patent disputes and bankruptcy. It ought to make the system less capricious. The Centre for Justice and Democracy, a pro-lawyer group, calls it “horrific”, which suggests it is worth a try. A Senate bill to allow pilot medical courts (among other reforms) may begin hearings early next year.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Lexington

A wise man in Washington

Dec 14th 2005
From The Economist print edition

Joe Lieberman may not be right for the Pentagon, but he deserves praise for putting principle above politics

IF THINGS had gone differently in Florida in 2000, Joe Lieberman might well be Al Gore's heir apparent, with “Joe-mentum” to win the 2008 Democratic nomination. As things turned out he is not in his party's throne-room, but in the dog-house.

The past couple of weeks have been particularly bruising for the junior senator for Connecticut. “I completely disagree with Mr Lieberman,” Nancy Pelosi, the party's leader in the House, says acidly. Jim Dean, Howard's brother and a Connecticut resident, is masterminding a signature-gathering campaign against him. The mullahs of MoveOn.org are accusing him of nothing less than betraying his party—and exploring ways of challenging him in next year's Democratic primary.

The cause of the latest round of thrashings is Mr Lieberman's renewed defence of the war in Iraq. On returning from his fourth visit to that country, he wrote a piece in the *Wall Street Journal* that took issue with the Democratic line that America is up a wadi without a paddle. In fact, he detected a plan that is beginning to work. A week later Mr Lieberman threw more petrol on the blaze by warning his colleagues not to play politics with Iraq. He quoted Arthur Vandenberg, a Michigan Republican who defied his party to support Harry Truman's policy of containment, to the effect that “politics must stop at the water's edge”. And he reminded his fellow Democrats that George Bush will be commander-in-chief for three more critical years: “In matters of war, we undermine presidential credibility at our nation's peril.”

It is easy to see why so many Democrats should regard this as a betrayal. Mr Lieberman has

sabotaged his party's (admittedly feeble) attempts to present a united front on Iraq, lent an aura of bipartisan support to Mr Bush's war and reinforced the Republican charge that questioning the war verges on the unpatriotic. Mr Bush and Dick Cheney both rushed to praise him. Donald Rumsfeld invited him to breakfast in the Pentagon. Now, to cap it all, rumours are flying that Mr Bush is preparing to dump Mr Rumsfeld in favour of Mr Lieberman in the new year.

Is Mr Lieberman really a serious candidate for the defence secretary's job? There is no doubt that Mr Rumsfeld is ripe for the boot: he is guilty of serial incompetence and he seems increasingly detached from his job. But bringing in Mr Lieberman would carry risks for both the president and the senator.

Mr Lieberman would certainly bring a new zest to making the case for the war at home—and, as a Democrat, he would reach voters who are suspicious of Mr Rumsfeld. But for Mr Bush, putting a novice in the Pentagon in the middle of a difficult war would be risky. And for Mr Lieberman accepting a job in the administration would mark the end of his career as a Democrat. There would be the immediate awkwardness created by the fact that his successor would be nominated by Connecticut's Republican governor. And even if a compromise could be reached on that, joining the hated Bush administration would kill Mr Lieberman's ability to shape the party that has always been his home.

Besides, you don't have to read the Pentagon tea leaves to explain Mr Lieberman's support for the war. It might sound like heresy in a town defined by the pursuit of personal gain and partisan advantage. But Mr Lieberman is speaking out because he thinks that it is the right thing to do. He may be wrong on Iraq, but he is not being treacherous or inconsistent.

He was a supporter of the idea that democracy is the only cure for the Middle East's proclivity for spawning terrorism back when Governor Bush was singing the praises of a humble foreign policy. He did as much as anybody in Congress to ensure the passage of the first Gulf war resolution in January 1991. He was a co-sponsor with John McCain of the Iraq Liberation Act in 1998. Shortly after September 11th 2001 he was one of ten lawmakers who signed a letter urging Mr Bush to target Iraq. His unflinching support for the Iraq war doomed his 2004 presidential campaign (he didn't manage to win a single delegate).

Mr Lieberman's hawkish position on Iraq is of a piece with his robustly centrist politics. He is an Orthodox Jew who champions the role of religion in the public square. He was one of the first Democrats to chastise Bill Clinton for his dalliance with Monica Lewinsky; he has also been a scourge of those who market violent films and video games to minors. He has been a consistent champion of both free trade and business (“You can't be pro-jobs and anti-business,” he argues). He was also one of the leading Democratic champions of welfare reform.

Clinton with a conscience

The hardliners in the Democratic Party no doubt regard this as an even bigger betrayal—a Republican-lite policy that will lead the Democrats to disaster. But Mr Lieberman has been a persistent critic of Republican positions on gun control and the environment, and he wants to raise taxes on the rich while lowering them on the middle class. His policies offer a much better recipe for Democratic success than the party's left. Like Mr Clinton in the 1990s, he understands that, as long as there are roughly twice as many conservatives as liberals, the Democrats will never win by appealing to their base, and they will certainly lose if they reinforce the public's suspicion that they are a bunch of cut-and-run, soft-on-defence doves.

Mr Lieberman is arguably the last surviving example of a peculiar Washington species: the Wise Man who is willing to put party allegiance aside when it comes to big issues such as foreign policy.

Figures like Vandenburg and Henry Stimson, who Mr Lieberman also mentioned in his speech, were commonplace during the second world war and the cold war. Pat Moynihan, Sam Nunn and Henry “Scoop” Jackson all preserved the wise man tradition in the Democratic Party. But today Mr Lieberman is almost alone in realising that there is more at stake in Iraq than just partisan advantage in the 2006 and 2008 elections.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Bolivia

A champion of indigenous rights—and of state control of the economy

Dec 14th 2005 | LA PAZ AND SANTA CRUZ
From The Economist print edition

Reuters

To the chagrin of the United States and eastern Bolivia, Evo Morales seems set to win the presidency. Whether he can win social peace is another matter

Get article background

IF EVO MORALES—coca grower, political street fighter and champion of indigenous rights—wins Bolivia's presidential election on December 18th it will be because of voters like Bernardino Montesinos. “The people want change,” says the former silver miner, who now sells lotions and shampoo out of a box in the centre of La Paz, Bolivia's capital. Foreigners have looted Bolivia's natural resources and traditional political parties “do nothing” for the people, explains Mr Montesinos. If Mr Morales becomes president, he will “nationalise everything” and supply technology that his silver mine lacked. An Aymara Indian, Mr Morales is “our blood.”

Bolivia is among the poorest of Latin American republics, and recently the most unstable. To Mr Montesinos and many like him, the election of the first self-proclaimed indigenous president would portend the overthrow of 180 years of oppression of poor, dark Bolivians by richer, whiter ones, and of Bolivia itself by foreign powers. Long feared by the elite, Mr Morales has won over part of the middle class, which is disgusted with corruption and hopeful that he will be less disruptive in office than he has been on the street.

Yet the promise of justice contains the threat of catastrophe. Unlike Brazil's Luiz Inácio Lula da Silva and Uruguay's Tabaré Vázquez, Mr Morales is not a leftist who has made peace with democracy and capitalism, offering change without upheaval. He is anathema in Bolivia's richer eastern provinces, which fear his plans to “bury the neo-liberal” state and “refound” the country by rewriting the constitution.

The United States is appalled: Mr Morales leads a union of coca growers, who produce the raw material for cocaine, and flaunts his friendship with Hugo Chávez, Venezuela's rabidly anti-American president. When he runs into resistance he will face a choice. Will he compromise, the only way to govern democratically? Or will he call on his supporters to take to the streets—the tactic which has brought him to the verge of power?

If the polls are right, Mr Morales will win the most votes but not an absolute majority. The newly elected Congress would then choose between him and his closest rival, probably Jorge Quiroga, a conservative former president. Mr Quiroga's negative campaign might just bring victory if anti-Evo voters defect from centrist candidates. Few people think Congress would dare deny Mr Morales the presidency if he leads on the popular vote. But his mandate may be narrow: he looks unlikely to gain the votes of much more than half of Bolivia's indigenous peoples.

Even if Mr Morales loses, the election will bring change. For the first time, Bolivians are electing *prefectos* (governors) of the country's nine departments who will give the increasingly assertive regions a powerful new voice. Until now, governors have been appointed by the president. The election marks the demise of nearly all the traditional political parties. Mr Morales's Movement to Socialism (MAS) is a confederation of unions and social movements, whose nucleus is his coca growers' union. Mr Quiroga is standing for a “citizens' alliance”, called Podemos.

Such changes will harden Bolivia's divisions. According to Carlos Toranzo, a political scientist in La Paz, the newly elected governors will call the shots in Congress, especially in the Senate, where the eastern regions are over-represented. Few if any will be from MAS. “Evo won't have the means to rule,” predicts Walter Guevara, an expert on Congress. Mr Quiroga would have more support from Congress and the governors, but would face the rage of the social movements, which have toppled two presidents since 2003.

To govern Bolivia, Mr Morales would have to deal adroitly with three hostile constituencies: the eastern provinces; private investors; and the United States. Yet any concessions to them will be opposed by the social movements. As a candidate he has dealt with this dilemma by pledging to “refound” Bolivia without saying how or what this might cost.

MAS will break Bolivia's reliance on commodity exports and extend development to those “historically excluded”, says Carlos Villegas, one of its economic advisers. The state will become the “fundamental axis” of development, financing small firms, promoting technology and backing big private firms “selectively”. Gas will be nationalised but the sanctity of contracts will be preserved. A MAS government will maintain stability, but the central bank should promote jobs as well as low inflation. It all sounds like a return to the policies that brought bankruptcy and hyperinflation to Bolivia in the 1980s.

As president, Mr Morales would have to make choices. Among the first will be how to deal with the new governors. Those from the east will push for broad autonomy, which could come only after a referendum and constitutional reform. Although some revenues were devolved in the mid-1990s, the central government still hires teachers, doctors and policemen; even local bus routes are laid out in La Paz.

Santa Cruz, gas-rich Tarija and other eastern provinces want these powers transferred to local government. Juan Carlos Urenda, a lawyer in Santa Cruz, says the centre's share of national revenue should be cut from three-quarters to a third. It can continue to set policy on land and natural resources, but the provinces should execute it. MAS backs autonomy in principle, but will balk if it means surrendering control of land or natural resources.

Gas guzzlers

Bolivia's economic prospects largely hinge on the government's handling of natural gas. Privatisation of the oil industry in the mid-1990s brought $3.5 billion of foreign investment, and the discovery of big gas deposits. The left claims it also stripped Bolivia of ownership of its most-prized asset and cheated the government of revenue. After weeks of blockades, in May Congress unilaterally increased royalties on gas output (raising $420m a year) and ordered energy companies to sign new contracts. Foreign investment has since plunged, with firms threatening legal action.

MAS wants to go further, but it is not clear where. Mr Villegas talks of restoring the state's power to set prices and to determine whether to export or keep gas for local consumption. That is part of the new law, although it has not been enforced. The government will negotiate with the gas companies individually, says Mr Villegas. “If we encounter absolute resistance, Bolivia has the sovereign power to make decisions,” he says.

The biggest uncertainty concerns MAS's plan to rewrite Bolivia's constitution in a constituent assembly starting in June. “The country will change at the constituent assembly and not before,” says Juan García Soruco, a MAS candidate for Congress. Its main business, apart from dealing with autonomy, will be to entrench the role of the state in the economy, redistribute land and secure indigenous rights. In the east, where farms are large, this raises the spectre of expropriation. Everywhere, it casts doubt on the rules that business must follow. “Would you invest before the constituent assembly?” asks Branko Marinkovic, who heads Santa Cruz's federation of private enterprise.

Ironically, if Mr Morales really wants to break Bolivia's dependence on commodity exports, his best bet may be the United States. Its trade preferences in labour-intensive industries like clothing and jewellery are worth $150m a year in exports and 100,000 jobs, many in El Alto, a restive city perched above La Paz. These expire at the end of 2006—a prospect that prompted a rare pro-American march last week.

On December 7th, Peru signed a free-trade deal with the United States; Colombia may follow. The United States wants to negotiate a similar agreement with Bolivia, rather than extend its trade preferences. It is also dangling $593m in aid to finance urgently needed infrastructure.

But these offers come with conditions. Foremost among them is a renewed effort to contain the growth of coca. That clashes with Mr Morales's pledge to “depenalise” the leaf (but not the drug). Many Bolivians are fed up with the United States' bullying drug “war”. But aid accounts for a tenth of Bolivia's GDP. Much of it is subject to American approval. If the United States “decertifies” Bolivia on drugs, markets and chequebooks could slam shut.

That would risk driving Mr Morales further into the arms of Venezuela and his own, impatient radical left. On December 10th a group of trade unions and social movements announced that he would have 90 days to “eliminate” the neo-liberal economy. Says Mr Montesinos, “if Evo lets us down, we'll throw him out, too.”

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Peru

Rise of another outsider

Dec 14th 2005 | LIMA
From The Economist print edition

Ollanta Humala feeds on discontent

The fewer policies the better

PERUVIANS have twice seen it before: a little-known outsider snatches the presidency from establishment rivals. In 1990, Alberto Fujimori, then an obscure university professor, defeated Mario Vargas Llosa, a novelist representing the traditional parties of the centre-right. In 2000-01, Alejandro Toledo, an economist of Andean Indian descent, brushed past more experienced rivals. So the sudden rise in the opinion polls of Ollanta Humala, a cashiered army lieutenant-colonel, has shaken the politicians.

In the past four months, support for Mr Humala has more than tripled to 22%, placing him second just three points behind Lourdes Flores, a conservative, according to Apoyo, a polling firm. It has done so despite daily media attacks on him, and although he lacks a manifesto. To some of his detractors, Mr Humala is a Peruvian version of Bolivia's Evo Morales (see article). Like Mr Morales, he has support among coca farmers. He is proof, the argument goes, that the Andean countries will fall, like dominoes, into the grasp of anti-*yanqui* radical populists owing cash and obeisance to the drug trade and to Venezuela's Hugo Chávez.

Yet Mr Humala is a very Peruvian phenomenon. He calls himself a “nationalist”; rather than a leftist, he is a military authoritarian. With his brother, Antauro, also a former army officer, he staged a military rebellion in the dying days of Mr Fujimori's authoritarian regime. Perhaps intentionally, this distracted attention just when Vladimiro Montesinos, Mr Fujimori's now jailed spy chief, fled abroad.

Antauro went on to form a movement of ex-soldiers which called for those accused of corruption to face a firing squad and the nationalisation of all industries. He is in jail, having staged a brief uprising in an Andean town on New Year's Day 2005 which left five people (including four police) dead.

Ollanta Humala now claims no political connection with his brother. His few policy statements have focused on reviewing contracts that grant tax breaks to foreign mining companies. With mineral prices sky-high, that is popular.

Mr Humala's support is concentrated among poorer Peruvians, and especially among those who still yearn for Mr Fujimori. They apparently see little benefit in democracy—although it allows them to vote for authoritarian leaders.

The election is not till April, and much can change. Unlike in 1990 and 2001, Peru's economy is growing steadily. This time, many Peruvians might feel that they have something to lose by

backing an outsider. If only, that is, the insiders put forward a more compelling case for democratic reformism.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD LATIN AMERICA

Cuba

An unsilenced voice for change

Dec 14th 2005
From The Economist print edition

A conversation with Oswaldo Payá

AFP

Payá, harassed but independent

FEW things endanger dictators as much as the free exchange of ideas. Maybe that is why Fidel Castro's communist government refused to allow Oswaldo Payá, Cuba's most prominent dissident, an exit visa to let him talk at a conference of European NGOs in London on December 8th. Mr Payá's treatment should cause European governments to reflect on whether their current policy of constructive engagement with Cuba makes sense.

Between 2001 and 2004, Mr Payá's movement gathered 25,000 signatures in a vain attempt to persuade Cuba's National Assembly to change the constitution to allow multi-party democracy. Activists of his Christian Liberation Movement made up more than two-thirds of the 75 dissidents and journalists rounded up and jailed for long terms in April 2003.

Unlike some other dissidents, Mr Payá refuses help from the United States. He opposes the American trade embargo against the island and the Bush administration's recent decision to set up a “Cuba transition” desk at the State Department. Speaking by telephone from the British embassy in Havana last week, he reiterated his commitment to peaceful democratic change. “We want to launch a transition programme within Cuba, one without revenge or radical leaps but rather one of reconciliation,” he said.

Mr Payá argues that most Cubans want democratic rights and freedoms. What holds them back, he says, is not just fear of the regime. They also fear change. For that reason, he says, a transition to democracy should not force ordinary Cubans to return their houses to the people who owned them before the 1959 revolution.

Most of Mr Payá's family are in exile. His house in Havana is watched by security police. He works as a technician in Cuba's health service. His prominence seems to offer some protection—in 2002 the European Parliament awarded him its Sakharov prize for human rights. The wives of the jailed dissidents were joint winners of the prize this year, but were denied exit visas to collect it this week.

This year, at the urging of Spain's Socialist government, the EU dropped the mild diplomatic sanctions it slapped on Cuba after the round-up of dissidents. An Ibero-American summit in Spain in October condemned the American embargo but said nothing about Cuba's lack of political freedom. Spain is “complaisant” with Mr Castro's regime, Mr Payá says. “We need a campaign of support and solidarity with peaceful change in Cuba” of the kind that brought an end to apartheid in South Africa and to the Pinochet dictatorship in Chile.

That is the message that Mr Payá would have delivered in London. It would have shamed all those in Europe who put their disagreements with American foreign policy above their support for Cuba's beleaguered campaigners for freedom.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Canada

Worm in the bud

Dec 14th 2005 | VANCOUVER
From The Economist print edition

A surge in gun crimes

CANADIANS love to boast that their society, unlike America's, is not crime- and gun-ridden. But hold on. In Vancouver, which regularly tops surveys of the world's most liveable cities, transport police were this month issued with handguns for the first time. Nightclubs use metal detectors to ban gangsters with guns. Almost every week sees a shoot-out outside a nightclub, or a gang member found slumped in his car with a bullet behind his ear.

Crime—and especially gun crime—is a growing concern in big cities across Canada. So far in 2005, Toronto has seen 50 murders involving guns—a record in recent years. Violence has become an issue in a federal election on January 23rd. Stephen Harper, the Conservative leader, wants stiffer sentences for drug trafficking, an end to plans to decriminalise marijuana and the closure of a safe injection site for heroin users in Vancouver. Paul Martin, the prime minister, has promised a sweeping ban on handguns (already tightly controlled) and C$50m ($43m) to fight gangs.

Yet few Canadians seem convinced that the answer lies in tougher laws or sentences. Much of the increase in crime is ascribed to organised gangs—and many of those are involved in the drug trade. A recent study by the Royal Canadian Mounted Police found that the number of criminal gangs in British Columbia has doubled over two years from 52 to 108—and they are more violent. Most trigger-happy are Punjabi-Canadian gangs, 60 of whose members have been killed in internecine warfare over the past six years. Once rare in British Columbia, the use of handguns is soaring. Police gun seizures have risen almost 50% in three years.

One prize is the province's homegrown cannabis business. This is worth perhaps C$7 billion a year—not much less than the tourism industry. The gangs export most of the weed to the United States, bringing back cash, cocaine and handguns.

Yet many Canadians recognise that repression alone will not prevent drug use. Vancouver is pioneering a public-health approach to drugs. Last month, the city council called on the federal government to legalise cannabis. The city strategy focuses on harm reduction, prevention and treatment as well as enforcement. With federal financial help, it has set up a pilot clinic prescribing free heroin to hard-core addicts, in addition to the safe injection site. These trials involve only about 750 of the city's 8,000 heroin addicts. Too few, say supporters. When it comes to dealing with drugs, and the violence that often surrounds them, the politicians seem stumped.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA

Japan's economy

Land of the rising price

Dec 14th 2005 | TOKYO
From The Economist print edition

Getty Images

But already there are tensions over tighter money

Get article background

THE most prominent feature of the mess into which Japan's economy had sunk after the bursting of its asset bubble a decade and a half ago was the country's grinding deflation: for the past seven years, prices have fallen relentlessly. So it is a momentous thing to contemplate the return of inflation, however mild, by the year's end. In October the “core” consumer-price index (ie, excluding fresh food) remained unchanged, compared with a year earlier, after a 0.1% fall in September. When figures for November come out later this month, they, too, will probably show prices unchanged or, whisper it quietly, even a tiny bit higher. But even if inflation is not to return in November, most economists say, then expect galloping inflation of 0.1% in December.

A cause for celebration, you would think, in an economy that is now showing ever more signs of pulling itself out of its long slump. Yet the only thing to be uncorked is an unholy row between the government of the prime minister, Junichiro Koizumi, and the central bank.

As the economy picks up, the Bank of Japan has been making it clear that the day is approaching when it will stop flooding the banking system with excess liquidity, a policy known as “quantitative easing” that was introduced in 2001 when interest rates that had been driven down to zero were still doing nothing to revive the economy.

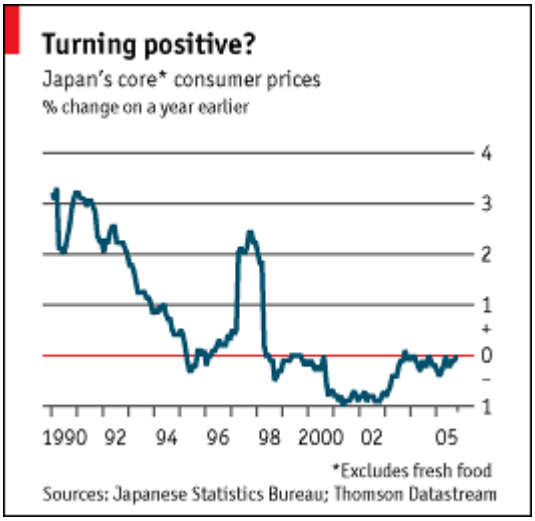
In particular, the Bank of Japan thinks that the output gap between what the economy can produce and what it is actually producing is narrowing quite fast, raising the prospect of imminent

inflationary pressures. The central bank is also worried that speculative bubbles might already be starting to form in some asset markets. The stockmarket, for instance, is up by one-tenth since the beginning of November, and by about 40% since the start of the year. So there are good reasons, the bank reckons, to prepare the world for an “exit” from a policy that targets the amount of liquidity sloshing around the system, in favour of adopting once again the more orthodox policy of steering monetary policy by setting interest rates.

A livid government, thinking such a move premature, has been hurling threats at the central bank. Heizo Takenaka, the new internal-affairs minister and Mr Koizumi's chief reformist ally, said recently that monetary policy was not the Bank of Japan's alone to make; should it end its policy of super-loose money, he added, then the central bank's independence, granted only in 1998, “could be discussed in the political arena.” Meanwhile, the ruling Liberal Democratic Party has just formed a new monetary-policy panel, headed by a fierce critic of the central bank, Kozo Yamamoto. The central bank is highly sensitive to criticism, given some big blunders in the past, especially when it raised rates in August 2000, way too soon.

Who is right this time? Certainly, the end of deflation is not assured. There is a risk that price rises will peak after the first quarter of next year, if the past effects of higher oil prices start to work their way out of the consumer-price index. The Bank of Japan forecasts inflation in the fiscal year to end-March 2007 of 0.5%: though at the optimistic end of the range of forecasts, it hardly provides much margin for error.

The government's chief concern, however, has to do with burden-sharing. Indeed, its alarm can be seen partly as a measure of its commitment to reforms which, while welcome in the long run, have a depressive effect in the short term. Mr Koizumi is committed to slashing debt issuance in order to plug a big budget deficit, while a hike in the sales tax looks increasingly likely in 2007. Plans for deregulation will also weigh upon economic activity in the near term. The government wants the central bank, with a loose policy, to carry some of the load. In particular, it does not want the bank to stop its huge monthly purchases of government bonds, equivalent to two-fifths of all debt issuance. A sudden end to those purchases would push bond yields up and, with them, the government's cost of servicing its debt. As it is, debt-service consumes 22% of the annual budget.



There are signs that the Bank of Japan, while asserting its intention to “exit” at some point, probably early next summer, is seeking to accommodate the government. Officials are at pains to say that it is possible to begin mopping up excess liquidity even as purchases of government bonds are kept up. Most important, they say that a return to a policy that targets interest rates does not preclude leaving them at zero for a long time—financial markets, for instance, do not now expect the first hike in rates until 2007 at the earliest. If inflation creeps back up, and interest rates do not change, monetary policy would actually get looser. That might be enough to mollify the politicians.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA

East Asian diplomacy

Dead on arrival

Dec 14th 2005 | KUALA LUMPUR
From The Economist print edition

A grand summit is a damp squib

“ONE vision, one identity, one community” was the wishful official slogan of a diplomatic extravaganza in Malaysia this week, bringing together the leaders of nations with half of the world's population. The first East Asia Summit was an ambitious attempt to create a common purpose among 16 countries ranging from impoverished despotisms to advanced democracies. But with two of the most powerful governments, Japan and China, not even on talking terms, the prospects were always going to be dim.

The East Asia Summit is intended to become an annual event, held in tandem with leadership meetings of the ten-member Association of South-East Asian Nations (ASEAN) and ASEAN+3, which also includes China, Japan and South Korea. But even its geographically inappropriate name reflects how little agreement there is about what this new group should be. The summit includes the ASEAN+3 countries, as well as three from outside the region: India, Australia and New Zealand. China had wanted something more strictly East Asian, while others, notably Japan, wanted the inclusion of countries that could dilute China's influence. The latter camp won, so the probability now is that China will quietly ignore the new forum, and concentrate its diplomatic energies on the more exclusive ASEAN+3 instead.

Besides, what was this unwieldy grouping supposed to achieve? Some speak of building a giant free-trade area, and even of promoting common values. But achieving consensus among such vastly different economies, cultures and political systems would be more arduous than anything encountered in regional community building elsewhere.

The 16 countries said that they would talk about “broad, strategic, political and economic issues of common interest”. But they agreed that ASEAN would be the “driving force” behind the new forum and that ASEAN+3 would continue to play a “significant role”. With ASEAN (which as a block is on good terms with China) as the hub of Asian summitry, China will have less to fear from the parallel development of a wider grouping including more of America's friends.

Chu Shulong of Tsinghua University in Beijing says that Chinese leaders now regard ASEAN+3 as the region's most important multilateral forum and downplay the new group's importance. The focus of China's efforts will remain establishing its own free-trade area with ASEAN. It is worth noting, though, that none of these configurations work particularly well: ASEAN's internal free-trade plans are lagging, and a plan to sign a deal with South Korea at the summit foundered over rice.

The wording of the summit's final declaration was an attempt to keep all sides happy by avoiding anything specific. It made no mention of establishing an East Asia community, or working towards a free-trade area. Nor did it specify the geographical boundaries of the grouping. Russia says it wants to take part in the next summit, to be held in the Philippines next December. But America is not angling for an invitation just yet. It is probably not yet sure whether it is worth being invited.

Overshadowing the summit were sharp disagreements between Japan and South Korea and China over a visit in October by Japan's prime minister, Junichiro Koizumi, to the Yasukuni Shrine, where Japan's war dead, including war criminals, are honoured. Normally, China, Japan and South Korea would hold a separate summit on the sidelines of the ASEAN talks. This time, because of China's ire, they held no meeting, though the prime ministers of China and Japan managed a chilly handshake at the end of the gathering.

In public, optimism abounded. The East Asia Summit “takes us on light years from where we've been,” said Helen Clark, New Zealand's prime minister. “It's important for political and security dialogue. It's important for understandings across civilisations.” But with a lukewarm China, those hoping for a European Union in the east will be disappointed.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

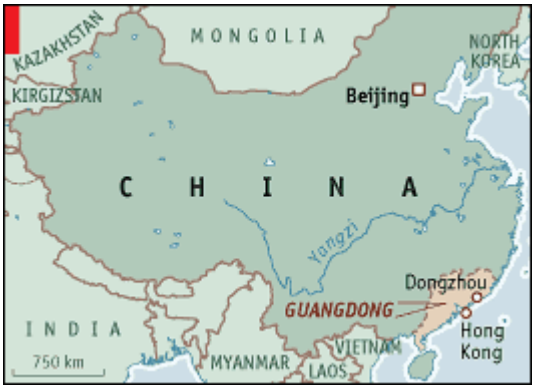
Economist.com WORLD ASIA

China

A demo turns bloody

Dec 14th 2005 | BEIJING
From The Economist print edition

But, for once, an admission of error



THERE was nothing at all unusual in the fact that hundreds of villagers in Dongzhou, in southern China's Guangdong province, launched a protest earlier this month after being forced to give up their land to make way for a new power plant. In today's China, where fast-paced growth keeps the economy humming but can also cause dislocation and discontent, such incidents have become common. Nor was it unusual that local security forces moved quickly to suppress the incident. As the frequency of such protests increases, the authorities are ever more fearful that unrest will spin out of control. The only thing that was unusual about the episode in Dongzhou was the way it ended on December 6th: in a volley of automatic-weapons fire by police.

Amid conflicting reports, the death toll remains unclear. Dongzhou officials say three people died, but local villagers have told the few foreign journalists to have made their way through roadblocks and into the town that as many as 20 were killed. If so, it could be among the most serious known use of force by Chinese authorities against civilians since June 4th 1989, when army units cleared demonstrators out of Beijing's Tiananmen Square, and killed hundreds—at least—in the process. In the nearly 17 years since then, China's government has never wavered from its insistence that it acted correctly on that fateful day. Indeed, it has always been deemed dangerous political heresy to suggest anything otherwise.

However, in yet another unusual aspect of the Dongzhou case, the government quickly admitted that “the commanding officer at the scene mishandled the situation and caused unintended deaths and injuries.” That unnamed officer, according to a government statement, now faces criminal prosecution. This move cannot but give other police commanders pause when they face decisions about how to handle unruly situations.

As many no doubt will: officials say that the number of “mass protests” taking place throughout China each year has risen from around 10,000 in 1994 to 74,000 in 2004. Although they have left a great deal unsaid about how these incidents are defined and counted, and how serious they are, it seems clear enough that their occurrence is on the rise.

So is China cracking under the strains of its breakneck growth? Not necessarily. Yu Jianrong of the Rural Development Research Institute of the Chinese Academy of Social Sciences—China's premier semi-official political think-tank—reckons that most protesters are agitating for the redress of very specific grievances, not because they want to overthrow the system. In the past these were often to do with the levying of unfair taxes, but more recently they have centred, as in Dongzhou, on inadequate compensation for the loss of land.

In an article early this year, Mr Yu said these conflicts do not by their nature “challenge the basic social structure” of China. The key, he said, will be whether the government is able to appreciate the significance of farmers' complaints. Rural conflicts will either “provide opportunities for reform” or “initiate social instability”. The ball, in other words, is in President Hu Jintao's court.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA

Australia

On the beach

Dec 14th 2005 | SYDNEY
From The Economist print edition

Race riots in paradise

AP

Wish they weren't here

Get article background

SPRAWLING along Sydney's southern Pacific shore, Cronulla beach has long symbolised Australia's laid-back way of life, a place where the sand and surf make everyone equal. That image was washed away on December 11th when a mob of about 5,000 mainly young, white Australians attacked a group of ethnic Lebanese, chasing, punching and pelting them with beer bottles. Police said they saved two of the victims from being killed. Next night, hundreds of Lebanese descended on Cronulla and nearby beach suburbs in revenge, firing guns and smashing cars with crowbars. Australia's worst racial violence in living memory shocked the country, leaving politicians perplexed about what it means and how to handle it.

The riot followed an attack the previous week by a group of young Lebanese men on two lifeguards who reportedly asked them to stop playing football on the beach. Lebanese youths visiting from outside Cronulla had already provoked the locals by sexually harassing young women. Now, an attack on lifeguards, the ultimate symbol of Australia's macho beach culture, was apparently too much to bear. Cronulla's mainly Anglo-Celtic population has not been submerged in Sydney's broader multicultural character. Its blond young men have waged territorial beach wars before, but never one with such a blatant racial character. This time, text messages called on “Aussies” to “reclaim our beach”. Fuelled by alcohol, chanting “No more Lebs” and waving seas of Australian flags, the rioters produced scenes that one Sydney newspaper judged “would not have been out of place in 1930s Munich”.

Their targets were hardly non-“Aussies”. The 19th-century merchants who comprised Australia's first Lebanese immigrants were followed by a larger group of refugees from the Lebanese civil war of the 1970s. Keysar Trad, a Lebanese spokesman for Sydney's Islamic community, estimates that

Sydney has about 500,000 people of Lebanese background among its population of 4m, most living in crowded suburbs north of Cronulla. Many children from the second wave of immigration identify strongly with their parents' homeland. But they suffer from high unemployment. Since Australia joined the war in Iraq, some young Lebanese have felt themselves to be targets of prejudice. They say the federal conservative coalition government's recent draconian anti-terrorism laws are really directed against them.

That may be far-fetched. But his opponents have been quick to link the Cronulla riot to a suspicion of Muslims that has existed ever since John Howard, the prime minister, won an election four years ago in part by exploiting hostility to boat people from the Middle East. At first, Mr Howard stayed silent about the riot. Eventually, he condemned it as “unacceptable” but denied that Australia was guilty of “underlying racism”. Cronulla lies at the centre of a suburban belt where Mr Howard has built a formidable political base that has kept him in power for almost ten years.

Morris Iemma, the Labor state premier of New South Wales, more bluntly described the riot as the “ugly face of racism in Australia”. He recalled the state parliament from holiday to give police stronger anti-riot powers. The way things are shaping, it will take more than that to bring peace back to the beach. And two attacks, on Lebanese families in Perth and Adelaide, may presage a yet wider problem.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA

Uzbekistan

After the horror, more horror

Dec 14th 2005 | TASHKENT
From The Economist print edition

Seven months after the massacre, President Karimov's grip is tightening

Get article background

ON HIS fourth visit to Russia since June, President Islam Karimov last month signed an unusually close mutual defence pact with his new best friend. It is believed to pave the way for Russia's intervention in any fresh uprising like the one in the city of Andijan in May, where up to 1,000 demonstrators were killed by troops. It may also coincide with the rumoured opening of a Russian base for special forces in Ferghana, close to Andijan.

Uzbek informants have noticed many new Russian-manufactured armoured personnel carriers suddenly appearing on a ring road near the capital. At the same time pro-American government ministers and officials are being replaced by pro-Russian ones, while Mr Karimov has followed up the official closing of the American base in his country by expelling NATO altogether and forbidding it from overflying Uzbek airspace. Outside pressure for reform, in other words, is all but dead.

Many Uzbeks feel powerless and afraid. The tiny opposition is under siege, freedom of speech is virtually non-existent, and pious Muslims are harassed. Only three independent journalists are still active—and one of them was assaulted a few weeks ago. The leader of a new political coalition (optimistically called “Sunshine”) was recently found in a prison cell, naked and incoherent, having apparently been drugged.

The worst conditions in the country are still in Andijan where hundreds of people are in jail. Some face serious charges, including those of premeditated murder and attempting to destroy the constitutional structure of the Republic of Uzbekistan, for their alleged role in the May revolt. They include a number of people who were wounded in the shooting. Some have had incriminating evidence planted. A continuing sweep of the area has seen several thousand arrested and intimidated. Trials of those accused of involvement in the uprising have been going on in camera in courts near the capital. Some 70 people have already been given prison sentences, but it is thought that the real figure is much higher and that more such secret trials are scheduled all over the country.

An interview with the father of one former prisoner speaks for many. Komiljonov Madumarov described, with remarkable composure, how his 28-year-old son, Shavkatjon, a respected imam working in Istanbul, ended up dead nine months after returning home for a holiday. Mr Madumarov said his son was charged with being a religious extremist—a Wahhabi. He was refused access to his family or to a lawyer. At his trial, in August, he complained to the judge that his health had swiftly deteriorated after he was forcibly injected with an unknown substance.

By then unable to stand, he was tied to a chair. When the judge failed to deliver a guilty verdict, for lack of evidence, he was replaced by another who did. Shavkatjon was given a six-year sentence. But four days after the verdict, he was dead. (The death certificate says: “cause of death: HIV infection”.) His body was returned in a heavy metal coffin, welded shut, and with 40

security men present to make sure the father didn't open it. Mr Madumarov wants an independent autopsy and retrial. Otherwise, he says, “I have no hope.”

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA

Thailand

The oracle of Lumpini park

Dec 14th 2005 | BANGKOK
From The Economist print edition

A talk-show host takes to the soap-box and embarrasses the prime minister

Get article background

Reuters

Tough times for Thaksin

EVERY Friday for the past six weeks, tens of thousands of people have gathered in Bangkok's Lumpini park to listen to criticism of Thaksin Shinawatra, Thailand's prime minister. The rallies began as a substitute for the weekly talk show that the organiser, Sondhi Limthongkul, had hosted on a government-run television station until its cancellation in September. Each week, Mr Sondhi has, in the flesh, unveiled fresh allegations of official corruption and misconduct, while the prime minister has retaliated with a series of libel suits. Mr Sondhi, who is also a newspaper magnate, now says he will settle for nothing less than the removal of the government. While that seems unlikely, the exchange illustrates how dramatically Mr Thaksin's political fortunes have ebbed since his landslide election victory in February.

The feud had been heading for a showdown at Mr Sondhi's most recent rally, on December 9th, for which he had vowed to assemble half a million protesters. But a few days beforehand, Thailand's revered King Bhumibol publicly chided Mr Thaksin for refusing to listen to criticism. The prime minister promptly withdrew all his lawsuits, thereby defusing Mr Sondhi's most potent charge, that Mr Thaksin does not show proper respect for the monarchy. Only a fraction of the 500,000 Mr Sondhi had hoped for showed up.

Nonetheless, the saga has proved embarrassing for Mr Thaksin, and not simply because of the king's rebuke. Despite the government's denials, Mr Sondhi's claims—that it ferried guests to Mr Thaksin's sister's birthday party on an air-force plane, padded the purchase price of luggage scanners for Bangkok's new airport, and usurped the prerogatives of the country's Buddhist patriarch, to name a few—have received wide coverage. Last month, Mr Thaksin's Thai Rak Thai party lost two by-elections, giving the opposition enough seats to table censure motions against ministers. It is already planning some related to Mr Sondhi's allegations. What with a recent court ruling that put the government's privatisation programme in jeopardy, street protests by disgruntled teachers and an insurgency in Muslim areas of southern Thailand, Mr Thaksin looks distinctly embattled.

The government still commands 375 of the 500 seats in parliament. It remains popular in the countryside, thanks in large part to Mr Thaksin's generous rural-development schemes. It also dominates the media: the only television station outside its control belongs to Mr Thaksin's family, Thailand's richest. Although breathless rumours of an impending coup have begun to circulate in Bangkok, there is little sign of discontent among the army or police. Mr Thaksin, after all, has been careful to promote friends and relatives to the top ranks.

But it is this concentration of power in Mr Thaksin's hands, argues Thitinan Pongsudhirak of Chulalongkorn University, that has helped galvanise opposition among middle-class Bangkok residents. Mr Sondhi's audiences, at any rate, seem excited just to hear someone stand up to the prime minister. Mr Thaksin, in response, seems uncharacteristically stuck for words. He will not speak to the media, he says, until Mercury moves into a more auspicious orbit next month.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Syria and Lebanon

The Syrians are in the dock, but the murders continue

Dec 14th 2005 | BEIRUT
From The Economist print edition

The UN's finger points at people close to Syria's President Bashar Assad

Get article background

THE metaphor was more fitting than its writer intended. “We have turned the day into a dark night,” said the fax posted by a hitherto unknown group claiming responsibility for this week's bomb that killed Gibran Tueni, a prominent Lebanese publisher and politician. The Arabic word for day, *an-Nahar*, happens to be the name of the high-brow Beirut daily that Mr Tueni's grandfather founded and his family still runs. Yet Mr Tueni's killing also darkened the cloud of deception and fear that has shrouded efforts to bring the light of truth into Lebanon's murky and dangerously polarised politics.

The most obvious of these efforts has been the UN-sponsored probe into last February's murder of Lebanon's long-serving prime minister, Rafik Hariri, which led to the withdrawal of Syrian troops and the ouster of the Syrian-run security establishment that had dominated Lebanon since its civil war ended in 1990. Few think it a matter of chance that Mr Tueni's assassination coincided with the release of a second progress report on this investigation, which, reinforcing an earlier report in October, suggests that people in the shadowy matrix of Lebanese and Syrian security services had Hariri killed.

With its Lebanese component now largely dismantled, most Lebanese tend to blame Syria for the 14 bombings that have shaken their country since February. These have now killed 13 people, including four leading Christians, among them Mr Tueni, who were outspoken critics of Syria's regime. Though not mandated to look into these later attacks, the UN investigation team, led to

date by a German prosecutor, Detlev Mehlis, cites new evidence in its latest report that a “high-level Syrian official” supplied arms to groups in Lebanon “to create public disorder in response to any accusations of Syrian involvement in the Hariri assassination.”

Mr Mehlis's report also politely but firmly chides Syria for stalling, despite a UN Security Council resolution obliging it to co-operate fully with the investigation. Syria did let five security men, now named as being among 19 suspects in the Hariri murder, be interrogated. But it also tried hard to discredit Mr Mehlis, most dramatically by televising a key witness's supposed recantation. The UN report suggests that this witness's original testimony was corroborated by others and retracted under duress. It also revealed that Syria claims to have burned all documentation of its 30-year armed presence in Lebanon, and has failed to produce two witnesses believed to be in Syrian police custody.

Mr Mehlis is retiring from the investigation team, but the UN Security Council may extend its mandate for six months. After requests from Lebanon's government, it may also broaden the investigators' brief to look into the post-Hariri bombings and set up an international tribunal to try the culprits. The council still refrains from imposing immediate sanctions on Syria for failure to co-operate, preferring instead to hold out the threat of “further action” under Chapter 7 of the UN charter, which authorises the use of force.

International wariness of hurting ordinary Syrians means that such punishment is likely, as a start, to be limited to restricting the movement of Syrian officials and diplomats. This would humiliate the increasingly isolated regime of President Bashar Assad but not bring him down. His mixture of bluster and delaying tactics followed by quiet concessions has impressed few outside Syria. Yet it has brought some sympathy from his own people: many remain persuaded by official posturing that presents their country as a bastion of Arab nationalism besieged by western and Zionist designs.

Such defiance plays well in other parts of the Arab world, including even Lebanon. Many Shia Muslims, the largest but historically most disenfranchised of Lebanon's 18 recognised confessional groups, still see Syria as the ultimate champion of the notion of “resistance”. Hizbullah, the strongest Shia party, sees the extension of UN influence in Lebanon as a Trojan horse for western domination. Pro-western Lebanese, particularly Christians such as Mr Tueni, are regarded as traitors for arguing that Hizbullah's “resistance” militia be disarmed, as demanded by the UN.

But acts such as the killing of Mr Tueni, while raising the spectre of the kind of tit-for-tat confessional response that led to a 15-year-long civil war, also strengthen the outrage that has fuelled a broad-based popular movement for greater freedom. Most Lebanese, including a growing number of Shias, are tired of being held hostage to outmoded heroic notions. What they want is the light of justice.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Iraqi Kurdistan

Taking the oil

Dec 14th 2005 | ARBIL
From The Economist print edition

Some things are so hard to share

AP

Let's have the oil as well as the water

Get article background

THERE are few more sensitive issues in Iraq than the control of its prized oil. So Iraq's Kurds were not surprised by the chorus of disapproval from their Sunni Arab compatriots at the news that a foreign company had begun drilling near the town of Zakho, in Kurdish-controlled territory near the border with Turkey. The result of a deal struck in 2004 between the Kurdistan Regional Government in Arbil, its capital, and a Norwegian oil exploration company, Det Norske Oljeselskap (DNO), the drilling heralds the first such project since Saddam Hussein's fall.

Long starved of what they say was their fair share of oil revenue under Mr Hussein and other previous rulers in Baghdad, the Kurds have been pressing hard to gain more control of natural resources in their region. Their prime minister, Nechirvan Barzani, declared at the opening ceremony: “The time has come that, instead of suffering, the people of Kurdistan will benefit from the fortunes and resources of their country.” DNO is one of seven exploration companies that have signed a memorandum of understanding with the Kurdish authorities.

This riles the Sunni Arabs, most of whom live in central Iraq, which is oil-free. The Kurds had gone behind Baghdad's back, they claimed. Saleh al-Mutlek, a prominent politician who heads a Sunni list in this week's election, gave warning that Kurdish leaders were thinking about seceding from Iraq. “That is why they began drilling the well,” he said.

In any event, it turns out that the Zakho deal was done with at least some knowledge of senior officials in the oil ministry in Baghdad. The canny Kurds were merely taking advantage of a grey

area in the constitution, which says that, while oil and gas belong to the whole country, regional governments as well as the federal one are responsible for managing oil and gas extracted from current fields. Oil income is to be shared out by quota, according to the population of each province, with extra cash going to areas particularly neglected under Mr Hussein.

A sheikh who belongs to the Muslim Scholars' Board, which influences some insurgents, says the Kurds are treating Iraq's oil as “war booty”. One reason why many Sunni Arabs voted against the new constitution in a referendum in October was the fear that its clauses on federalism would let regional governments control any new oil fields, so cutting off funds for their oil-poor region; the Kurds say there are ample reserves in the Sunni area west of Baghdad, but they are unproven.

Crucially for the Kurds, the constitution does not mention new exploration in existing fields. Article 111 provides for regional governments to control everything that is not exclusively ascribed to the federal government. A new oil and gas law will go before the new national parliament after this week's general election. It may well present the new government with its first constitutional crisis.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Iran

Sex rears its head

Dec 14th 2005 | TEHRAN
From The Economist print edition

The ruling clergy comes clean, almost, about how you can get AIDS

Get article background

HOW should a theocratic state that claims to have realised the ideals of the Prophet Muhammad raise awareness of a lethal virus that is commonly spread through sexual promiscuity, a sin the authorities say they have all but eradicated? Under its first anti-AIDS strategy, unveiled in 2001, the Islamic Republic of Iran reached out to the intravenous drug users that made up the majority of Iranians hit by HIV or AIDS, but piously ignored the danger posed by a recent rise in prostitution and casual sex. Dr Hamid Amadi, one of the country's top AIDS specialists, likens this to dousing flames with burning ash.

Partly thanks to the provision of clean syringes for heroin addicts, many of whom languish in Iran's teeming jails, the official number of HIV cases has been kept to a relatively low 60,000 in a population of around 65m. But Iran's famously secretive culture means that the real figure is probably far higher. On the subject of sexual transmission, which Dr Amadi expects to become the main carrier for the virus in the current decade, the authorities are still in denial.

Iran's marking of World AIDS Day, earlier this month, was a case in point. At a seminar attended by a top UN expert, health officials assiduously played down the prevalence of sexual transmission in Iran, in contrast to the decadent West. Nearby, schoolchildren watched a celebrity football match and listened to speeches by famous sportsmen; none alluded to the ways AIDS is transmitted. Less than 10% of 15-24-year-olds have what a recent study described as “an accurate knowledge” of the disease.

A tour of Tehran after dark may be the best education. A startling number of the capital's residential street corners are frequented by prostitutes. Some parties held by rich kids are renowned for their sexual audacity. In a reaction to what many regard as pervasive moral decline, Iranians voted in an ultra-conservative, Mahmoud Ahmadinejad, as president this summer; many of them agree with the government that, when it comes to sexual conduct, Islam provides all the answers.

The result is a baleful opacity of purpose. Though it disapproves of NGOs as a pernicious western invention, the government is letting new anti-AIDS NGOs start up. The health ministry has even approved a UN pamphlet, to be distributed to universities, that discusses sexual practices which could lead to infection. But any doctor who dares canvass information about sexual mores among the young may be hauled before the courts for promoting vice, and the government has put on hold plans for a timid sort of sex education in schools.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD AFRICA & MIDDLE EAST

Israel's Supreme Court

Who should make the law?

Dec 14th 2005 | JERUSALEM
From The Economist print edition

A row over judicial appointments goes to the heart of a secular-religious divide

THE intense politics and extravagant lobbying surrounding Supreme Court nominations in America have been absent in Israel—up to now. In America they go back to 1987, when Democratic senators savaged Robert Bork, a conservative nominee of Ronald Reagan, giving rise to the verb "to bork". Now Israel has its own Mr Bork. But the dispute goes to the heart of several long-running debates about what kind of state Israel should be and what kind of justice system it should have.

Ruth Gavison, a law professor at the Hebrew University who is up for one of three vacancies on the court, is controversial first for her apparent shift in politics. In 1994, when president of the Association of Civil Rights in Israel, the lobby won a landmark Supreme Court case granting same-sex partners of company employees the same benefits as opposite-sex ones. Yet in 2003 she published a "covenant" with a right-wing rabbi, Yaacov Medan, that tried to mend the rift between secular and religious Israelis by setting down principles for a modern Jewish state. It included a proposal to institute civil marriages, but for heterosexual couples only. At present, Israeli Jews can be married only by a rabbi, so many have a secular marriage abroad instead. Some of her former civil-rights colleagues accuse Ms Gavison of betrayal.

Yet her politics is overshadowed by her other main belief: that judges should, in any case, leave a lot more to politicians to decide—including what kind of marriage is legal. This don't-legislate-from-the-bench philosophy, reminiscent of Mr Bork's, is much more controversial since it challenges the "everything is justiciable" maxim of the Supreme Court's president, Aharon Barak. Under him, the court has broadened its remit in several areas. Most notably, it began treating Israel's Basic Laws, a sort of partial constitution, as if they were a real constitution, and has used them as a basis for junking other laws. Ms Gavison argues that no other court in the world has simply given itself such powers without a written constitution. She also thinks that since judges are appointed by a panel of nine that includes five jurists, rather than by politicians alone, it is too unaccountable to have the power it claims.

Conservatives often argue for liberal courts to have their wings clipped, and vice versa. Ms Gavison declined to comment on whether her two sets of views are connected. Israeli liberals, though, argue that only such an activist court could have achieved many of Israel's main civil-rights advances (for years its positions on gay issues, for instance, were among the world's most progressive) and curbed some of the most egregious abuses against the Palestinians. Next year it is to rule on whether same-sex marriages performed abroad should be recognised in Israel as opposite-sex ones are, and will probably say yes. That too would go against the Gavison-Medan covenant.

Yet the main reason for the furore is that Mr Barak is due to retire next year. So Ms Gavison, though not up for the court's presidency, would represent the first serious challenge in years to its basic premise. Some judges, says Alon Harel, a fellow law professor, may also feel challenged by the fact that "Ruthie is a brilliant jurist—there is nobody like her today on the court." Even some

jurists who disagree with both her politics and her judicial philosophy think she should be on the bench, if only to keep the court on its toes.

Last week the Israeli Bar Association elected its two representatives to the judicial-appointments panel, one of whom opposes Ms Gavison. That seems to tip the balance against her. But the fight is not over. It is unclear whether the panel can meet at all, with a general election in March. If it waits, the politicians on it will change, perhaps shifting the balance again, amid frantic deal-making. Even if Ms Gavison does not get the job, says Mr Harel, the naming of judges in Israel is destined, as in America, to become noisy.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Ethiopia and Eritrea

Big brother has other worries

Dec 14th 2005 | ADDIS ABABA AND BOSSASO
From The Economist print edition

Ethiopia backs down, for now

WAR between Ethiopia and Eritrea was averted this week, at least for a while, when Ethiopia agreed to pull its troops back from its disputed border with Eritrea. That was after considerable pressure from the UN, which is determined to prevent a repeat of the grisly trench warfare which ended inconclusively in 2000, with 70,000 lives lost.

It was canny of Ethiopia, much the bigger of the pair, to run for the high moral ground just when Eritrea was being cudgelled forward by its dictatorial leader, Issaias Afwerki, who promptly denounced Ethiopia's move. Earlier he had expelled all UN peacekeepers whose countries he dislikes: a long list. But then the border struggle is an absolute for Eritrea, while for Ethiopia it is only one of several pressing concerns.

Indeed, Ethiopia's prime minister, Meles Zenawi, may have pulled back in part to divert attention from his government's treatment of its political foes. Mr Zenawi admits “several thousand” opposition supporters are detained in camps after recent political disturbances. Some say the figure is 40,000. Several of the detention camps, including Bir Sheleko in the north-west and Didesa in the malarial west, may hold 10,000 prisoners each. Access is restricted, but there have been reports of disease, hunger, maltreatment and possibly even torture.

Some opposition MPs have taken up their seats in parliament, ending a boycott, but in private some say they have done so only after harassment from plain-clothes security police. Several opposition leaders, imprisoned on treason charges after the disturbances, have gone on hunger strike. Their condition is not widely reported. Non-government newspapers are still being published but their reports have become warier since 15 journalists were put behind bars.

Young urban Ethiopians are particularly afraid. Hundreds of university students, mostly from Addis Ababa, the capital, are sleeping rough in the streets of Bossaso, a port in northern Somalia, with little money and nowhere to go. Many show their opposition party membership cards. They have fled, they say, in fear of their lives.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Somalia

A state of utter failure

Dec 14th 2005 | GAROWE AND JOWHAR
From The Economist print edition

A few glimmers of hope that Somalia may one day be re-invented

Get article background

TO MOVE cash the few score miles between Mogadishu, Somalia's lawless official capital, and Jowhar, the seat of its transitional government, a local money-vendor has to pay $6,000. For that he gets an armoured lorry, 30 gunmen and three “technicals”—jeeps with heavy machineguns. What he doesn't get is insurance or any recourse to a state authority if his gunmen are killed, for state authority does not exist. But the money vendor still moves the cash, if the amount is big enough, and still makes a profit.

Somalia is resilient. Consider its amazing currency, the Somali shilling, which has operated for 14 years without a central bank or reserves of any kind, save the will of ordinary Somalis. Though the country has lacked a government, it has never quite ceased to exist. But for all that, Somalia remains Africa's most utterly failed state, as it has been since 1991, when it fell to pieces after tribal militias toppled a dictator, Mohamed Siad Barre, then turned on each other. Since then, the place has been torn apart by rival warlords, leaving at least 300,000 dead. The outside world virtually gave up on the country after a disastrous American-led UN intervention ended with the deaths of 18 American troops and perhaps 1,000 Somalis after a ferocious battle in Mogadishu in 1993.

But though the world may have tried to forget Somalia, the country refuses to forget the world. Its anarchy has made it a perfect environment for small but dangerous groups of terrorists and bandits to hide out in. Somali pirates have attacked dozens of ships off the central and southern

coast, including a cruise liner and UN food ships. Jihadist groups linked to al-Qaeda have also flourished, murdering, among others, foreign aid workers and journalists. Somalia's capacity to export its violence worries both the West and closer neighbours. The interior minister of Yemen, across the Red Sea, says Somalia is “like Afghanistan before the Taliban took over”.

So the tentative success of its latest transitional government, led by a widely disliked but tough former warlord called Abdullah Yusuf, has to be an encouraging sign. There have been no fewer than 13 previous attempts to form a government since 1991: Mr Yusuf's, backed by the European Union, is number 14. He may still be confined to Jowhar, unable to move to, let alone exert any influence over, the ostensible capital, Mogadishu, but his government is already the longest-lasting of all of them.

If peace holds for a little longer, Mr Yusuf may start to look a little more like the real thing. Parliament might even meet, and proper elections be held in 2009. The danger is that opposing factions in Mogadishu, angry at being excluded from the government and worried that their roadblocks and other sources of revenue may be curtailed, may choose to fight it out instead. A rebel force rolled out of Mogadishu a fortnight ago towards Kismayu, a southern port. The warlords in charge of the forces say they mean to negotiate with Mr Yusuf in a neutral town, but doubters say they mean to fight.

If the two sides do come to blows, in Kismayu or farther north, it could be some of the bloodiest fighting since the 1990s. Mr Yusuf probably needs some 10,000 troops for a march on Mogadishu, but has only about 4,000—and is short of cash to pay this “national army”. Foreign donors are loth to give more money until the parliament has met a few times, which, in the short run, looks unlikely.

So not everyone is putting their hopes in Mr Yusuf's administration, least of all the Americans, who fear that Somalia may become another incubator of international terrorism. “It's a truck bomb,” says one diplomat. “It's not a matter of if it goes off, but when.” The United States dislikes the formula for dishing out seats in the new parliament (61 each to four large clans, 31 seats to the rest), saying it is too clunky. It also says that Italy, the former colonial power in most of the country, and Ethiopia, Somalia's neighbour to the west, which has a population of 70m to Somalia's 8m, have primed the bomb by favouring the Jowhar faction and its associated clans over the Mogadishu faction and its even more intricate web of clans, sub-clans and Islamist mavericks.

Some American officials privately say that Italy, despite a UN ban, is funnelling arms to Jowhar through Ethiopia. Italy angrily denies this. America, after all, has no one on the ground and no intention of sending anyone, save a few counter-terrorism agents chasing al-Qaeda suspects. In contrast, the Italians are busy on the ground—and more knowledgeable. It makes sense, they say, to go with the “centre of gravity”. The British and other EU countries are somewhere in the middle, supporting the Jowhar faction but trying to keep the Mogadishu lot on board too.

The main hope for peace lies in the northern parts of Somalia: in Somaliland, which used to be a separate British colony, and is now relatively peaceful and well governed, and in Puntland. Somaliland has in effect seceded from Somalia, and yearns for full legal independence. Puntland, Mr Yusuf's own stronghold, which was the northern part of Italian Somaliland, is now pretty autonomous, but its leaders prefer to see Puntland as a building block for a future federal Somalia.

Meanwhile, the rest of the country is wretched. Most people are illiterate. Only 18% of children go to primary school. Garowe, Puntland's dusty capital, is swollen with migrants from the south. Its slums are spreading, the wells are contaminated, cholera occasionally breaks out, and polio has reappeared. Habitat, a UN agency that tries to provide housing and shelter, is struggling to bring some order here and in other Somali towns.

But it is more trade, not aid, that might improve things the most. Saudi Arabia could help by restoring its imports of Somali livestock that were stopped in 2000, and Somalia needs help developing its offshore fishing waters, which are being plundered by foreign boats.

Don't forget us

While nearby countries such as Uganda, Sudan and Ethiopia get billions of dollars of aid in cash and kind, plus massive attention from diplomats seeking to bring peace to the region, Somalia is still largely ignored. Yet the risks of failing to find and bolster a government that commands a degree of national unity may outweigh the risks of getting entangled again. The International Crisis Group, a Brussels-based think-tank, says that jihadists will gradually make headway among Somalia's despairing and disaffected citizenry. “It will only be a matter of time”, it says, “before another group of militants succeeds in mounting a spectacular terrorist attack against foreign interests in Somalia or against one of its neighbours.”

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD EUROPE

France and immigration

After the riots

Dec 14th 2005 | PARIS
From The Economist print edition

Getty Images

The politicians manoeuvre, but they come no closer to solving the problems of integrating the country's ethnic minorities

Get article background

“FRANCE is a great nation. Its past was glorious.” “France is a great country, because it has a great history.” They sound like the incantations of a long-forgotten emperor, but in fact they are declarations by those who govern France today: the first by President Jacques Chirac, the second by Nicolas Sarkozy, his interior minister. That France's politicians feel the need for such rousing rhetoric is testimony to how far the country has, after the riots, plunged into a collective depression.

The latest round of self-criticism was set off by a failed attempt last month by the opposition Socialists to repeal a law requiring school textbooks to “recognise in particular the positive role of the French presence overseas, notably in North Africa”. The law was pushed by members of the ruling UMP party from the south of France, home to many *pieds noirs* (former French settlers in Algeria) and *harkis* (Algerians who fought for France). Although the law passed without a murmur in February, the Socialists have belatedly cried foul, denouncing this attempt to impose the state's preferred version of history.

Such was the fury that Mr Chirac made a rare televised address to calm tempers. He promised a commission to study parliament's role in the construction of memory and history. This week he added his support for a day to remember slavery. Both he and his prime minister, Dominique de Villepin, have distanced themselves from the February law, insisting that history is a matter for historians, not lawmakers. This has cast Mr Sarkozy, who cancelled a trip to the French West Indies last week after protests against the new law, as its chief defender. He has railed against the

“excessive repentance” of the French intelligentsia, arguing that “when one walks around Algiers, one realises that one cannot reduce the French presence to torture.”

Behind this unexpected debate over the virtues of France's colonial past lie two struggles. The first is a fratricidal war on the political right, which has intensified since the riots in the *banlieues*. The second is the country's difficulty integrating the children of ex-French colonies, so vividly exposed by the riots.

On the first count, the commotion is in some ways yet another row that pits Mr Sarkozy, who heads the UMP, against those from whom he wrested control of that party: Mr Chirac and his protégé, Mr de Villepin. Electorally, the right may gain from the riots, since security fears play to its strengths. But Mr Chirac himself, already enfeebled by the French rejection of the European Union constitution last May, has been further marginalised. A devastating poll in the *Journal du Dimanche* has suggested that only 1% of French voters want him to seek re-election in 2007.

The contest between his two would-be successors on the right, though, has only just begun. Mr Sarkozy remains the favourite. In the same poll, 36% backed him, against 19% for Mr de Villepin. With his tough-talking ways and his action-man style, Mr Sarkozy has earned a reputation for zero tolerance. With his promises to expel foreign criminals, he has broadened his appeal to far-right voters. Last week, he sealed his grip on the party machine by ensuring that the UMP would back a single candidate for 2007: the party, as one observer puts it, has been *déchiraquisé*.

Yet Mr Sarkozy's success is not guaranteed. A separate poll by Ifop ranked him as only the fourth most popular politician on the right. Mr de Villepin came top, with a seven-point lead. UMP deputies know that the prime minister has wider appeal to the centre and the left, making him a better second-round candidate. In some ways, the row over colonial history suits the *chiraquiens*: the more Mr Sarkozy leans to the right, the more space there is in the centre for Mr de Villepin.

A second underlying conflict helps to explain why the textbook row has touched such a raw nerve: the post-riots debate over integration. The left, which admits it was dozing in February, now argues that the textbook law is provocative and wounding for France's ex-colonies and their descendants, at a time when France cannot afford to stigmatise its minorities. Aimé Césaire, a 92-year-old writer from Martinique who has long advocated “negritude” as a response to colonial humiliation, was one of those who refused to see Mr Sarkozy. François Hollande, the Socialist leader, said the law was a “disaster” and would further ostracise those of immigrant origin.

A month after the riots died down, France is still taking stock. In three weeks of violence across the country, some 10,000 vehicles were burned, 255 schools, 233 public buildings and 51 post offices were attacked, 140 public-transport vehicles were stoned, and 4,770 people were arrested, according to figures obtained by *Le Monde*. A report by the Renseignements Généraux, the police intelligence service, leaked to *Le Parisien*, concluded that the violence was neither orchestrated nor religious, but was rather a “popular revolt” linked to a “crying lack of integration”. It gave warning of possible fresh explosions on New Year's Eve, when hundreds of cars are torched even in normal years.

In response, a raft of policies is being drawn up. These include tougher controls on unemployment benefits, a crack-down on drug mafias, tighter checks on forced marriages, tax breaks for businesses relocating to the *banlieues*, apprenticeship schemes for teenagers and extra money for local associations.

Among the most interesting ideas is a new effort to promote ethnic minorities. After the riots, Mr Chirac spelled out for the first time that he wanted France's institutions to reflect its population—but to do it while remaining officially colour-blind. As Mr de Villepin put it on CNN, “we don't want to take into account the colour of the skin, or the religion.” This directly counters Mr Sarkozy's

preferred idea of affirmative action for minorities. The French have been tying themselves in knots to work out how to promote diversity (good) without legitimising racial categories (bad), which to republican French ears smack of apartheid and infringe civil liberties.

There are some signs that France is reaching for a compromise. Azouz Begag, the minister for equality (who is of Algerian origin), is one of the few who argues that “we must measure the presence of the children of immigration in the police, magistrature, administration and the private sector.” He suggests using the birthplace of parents and grandparents as a proxy. Social scientists sense a first chance to study a subject that has hitherto been taboo. Nobody is fooled that such ethnic monitoring would solve the difficulties of integration. But it would at least unveil their extent, and offer a way to measure progress.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Balkan history

A better view of the bad guys

Dec 14th 2005
From The Economist print edition

The perils of teaching more than one view of history

WERE the Ottoman rulers of the Balkans tyrants, or relatively benign protectors? The first, of course, in the history that most Serbian, Greek or Bulgarian children have long been taught. For them, the centuries of Ottoman rule constituted a dark night of oppression of Christians who retained their faith and culture only by tenacity and cunning—until the time came to throw off the oppressors and live happily ever after.

In Turkey, and among the Muslims of Bosnia, Balkan history is viewed from the opposite side of the looking-glass. Compared with most regimes in western Europe, the Ottomans were generous and tolerant towards minority religions and languages—until their ungrateful Balkan subjects rose up and slaughtered every Muslim in sight.

More recently, there is the sensitive issue of how the people of Yugoslavia responded to Nazism. Was Cardinal Aloysius Stepinac, spiritual leader of Croatia's Catholics, an unabashed supporter of a murderous fascist regime, as communist Yugoslavia said? Or was he a saintly fighter for religious freedom, as the Vatican now insists?

Many grown-up historians would say that, on questions like these, there is room for reasonable people to disagree—and that the truth might lie somewhere in the middle. Now, for the first time, the children of south-eastern Europe may be getting a chance to see history from more than one point of view.

After seven years' work by scholars from around the region, a set of “objective” history manuals—on the Ottoman era, the Balkan wars of 1912-13 and the second world war—have been produced (and are now being translated into ten languages) by the Centre for Democracy and Reconciliation in Southeast Europe, a Salonika-based think-tank. Education authorities in Kosovo and Croatia are keenly interested, but the first country to incorporate the books into its school system is Serbia. Its education minister, Slobodan Vuksanovic, says that they are the first teaching materials he is not ashamed to show to his teenaged daughter.

The authors say they have had a warm response from teachers all over the region. But presenting history from more than one viewpoint is still a hard sell. For communist teachers, the villains are always fascists and feudal overlords. According to nationalist history, a whole nation—rich and poor, landlord and peasant—rises against a bad regime (and its local lackeys) and heroically prevails. Even if neither story turns out to be true, or even half-true, children still want to know: who were the bad guys?

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD EUROPE

The Balkans and Europe

Testing times

Dec 14th 2005
From The Economist print edition

Why nerves are jangling from Croatia to Macedonia

FOR the countries of former Yugoslavia, 2006 will be busy—and perhaps dangerous. This time next year, the map may look quite different. In Kosovo, there is a risk of violence linked to talks over the province's future status. Montenegro will bid for independence. As all countries in the western Balkans prepare for talks to join the European Union, one source in Brussels talks of “a giant ‘to-do’ list”.

Last week's arrest of Ante Gotovina, a former Croatian general, has at least crossed one item off the list. Mr Gotovina was the only Croat fugitive still wanted by the UN's war-crimes tribunal in The Hague. He faces charges of murder and ethnic cleansing during the operation to end Serb rule in Krajina in 1995 that saw the flight of up to 200,000 Serbs. That he was picked up in Spain, after a tip-off from the Croatian government, suggests that it has at last regained control over its security services, which have helped Mr Gotovina in the past. The threat of suspending Croatia's talks on EU accession, which began in October, for failure to co-operate with The Hague tribunal has now been lifted.

Such a threat still hangs over Serbia and Montenegro. All six remaining fugitives from The Hague are Serbs. It seems more than likely that some parts of the country's security services know the whereabouts of the two biggest fish, Radovan Karadzic, leader of the Bosnian Serbs in the war of 1992-95, and Ratko Mladic, his military commander.

In October Serbia and Montenegro began talks on a Stabilisation and Association Agreement with the EU, a prelude to membership talks. With Mr Gotovina behind bars, pressure to find the other fugitives will increase—and, if the Serbian authorities are not judged to be doing enough, the talks could halt. They may in any case have to pause for the country to disintegrate. A commission of the Council of Europe has just written a draft opinion finding Montenegro's referendum law

acceptable. Montenegro may hold its vote next April. If the opposition boycotts it, independence (and instability) may be the result—though, with luck, not violence.

Few would be so sanguine about Kosovo. Since the end of the war in 1999, it has been under the jurisdiction of the UN even though it is technically part of Serbia. A large majority of its people, over 90% of whom are ethnic Albanian, want full independence. Serbia's leaders are against. A UN-led group under the leadership of Martti Ahtisaari, a former Finnish president, has now started discussions on Kosovo's future status. He may recommend “conditional independence”, ending the sovereign link with Serbia and offering a form of independence to Kosovo, but with residual powers being given to an international mission that would take over from the UN.

The EU does not want to run Kosovo but it knows it must play a big role in its future and may have to pay a lot of the costs of running the place. Javier Solana and Olli Rehn, respectively the EU's foreign-policy supremo and its enlargement commissioner, have begun planning. In a recent letter to colleagues, they have given warning of the need to make “adequate” provision for Kosovo, although nobody knows how much it might cost.

Equally, nobody knows what would happen if the “disaster scenario” struck, with the talks led by Mr Ahtisaari stalling and hard-line Albanian (or Serb) nationalists provoking violence. That could conceivably lead to the flight of the province's entire Serbian population of 100,000 people (out of some 2m). As one western diplomat says, “we're terrified silly.”

Meanwhile Macedonia, which in 2001 almost descended into civil war between the majority Macedonians and minority ethnic Albanians, is on tenterhooks. Only the prospect of EU membership now holds the country together. This week's EU summit will decide whether to give Macedonia the prize of candidate status. In advance of the meeting, France has signalled its opposition, on the grounds that the EU needs to sort out its budget and future direction before expanding any more. That may just be negotiating tactics, but a failure to win candidate status would be a heavy blow for Macedonia—and for the rest of the western Balkans, which will be watching the Brussels summit unusually closely this week.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Germany and Russia

Jobs in the pipeline

Dec 14th 2005 | FRANKFURT AND LONDON
From The Economist print edition

Germany's ex-chancellor takes a juicy job—and plenty of flak

Reuters

Schröder gives himself a hand

AS A KGB officer in Germany during the cold war, Vladimir Putin was expected to recruit gullible or greedy locals to the Soviet cause. Watching the growing love-in over the past five years between him and Gerhard Schröder, then Germany's chancellor, some cynics wondered if Mr Putin's old skills were still at play in his new role as Russia's president.

Such thoughts could surely be dismissed as insulting. If Germany was treading on its eastern neighbours' sensitive toes in its enthusiasm for deals with Russia, that was a matter of realpolitik about new gas supplies. “I am the German chancellor, and I have to represent German interests, particularly regarding energy security,” declared Mr Schröder at a news conference with Mr Putin in September.

The German leader was responding to criticism by Poland and the Baltic states about a new gas pipeline under the Baltic sea. This would allow Russia to supply western Europe while, in theory at least, cutting off its former satellites. Russia says that a direct link is essential to avoid the risk and cost of transit over unreliable third countries. Critics say it will be the longest and most expensive gas pipeline ever built, with big ecological risks.

Now Mr Schröder's defence of the pipeline plan is looking tainted with self-interest. Within weeks of stepping down as chancellor last month, he has taken the job of chairing the pipeline consortium's shareholder committee, at an annual salary, claims *Bild am Sonntag*, a Sunday tabloid, of some €1m ($1.19m). He says the sum is much less.

The new Christian Democrat-led grand coalition government under Angela Merkel supports the pipeline. It hopes to make the project more palatable to the Balts and Poles, perhaps by guaranteeing branch pipelines to their own networks. Ms Merkel and Brigitte Zypries, her justice minister, have not condemned Mr Schröder. But they have floated the idea of a voluntary code for

senior politicians, along the lines of a 2003 corporate-governance code.

Some of Mr Schröder's political allies, such as Matthias Platzeck, the new boss of the Social Democrats, and Klaus Wowereit, governing mayor of Berlin, are behind him. So are BASF and E.ON, the two German members of the pipeline consortium. He can use his contacts to get things going, said a BASF spokesman. But that may be a risky line, as the project's backers like to insist that it is purely a business deal, with no political dimension.

The new job has prompted outrage right across the political spectrum. Some of the harshest criticism of Mr Schröder has come from Christian Wulff, the Christian Democrat premier of Lower Saxony, who called on him to change his mind—or at least to reveal how much he will be paid. Markus Meckel, a foreign-affairs specialist from Mr Schröder's own Social Democrats, says the appointment is “problematic” and “leaves a bad taste”. He blames Mr Schröder for portraying the project in terms of the national interest, rather than wider energy security.

Besides damaging his political reputation, Mr Schröder may find he has legal problems. The pipeline company is based in Switzerland and not publicly traded, so there are no corporate-governance issues. But some lawyers say that Mr Schröder may have to prove he is not infringing the German criminal code. Section 331 bans the procuring of private advantage from public office, so Mr Schröder may need to show that he did not discuss his new job as chancellor. Section 353b on the protection of state secrets poses another problem. Could Mr Schröder use confidential information gained while chancellor to help the pipeline consortium? “He may at any time be asked to prove this is not the case,” says Peter-Alexis Albrecht, a criminal-law professor at Frankfurt University.

When he was chancellor, Mr Schröder was known as the *Genosse der Bosse* (the “tycoons' comrade”). He now looks set to retain this tag, even in retirement. And the next time east Europeans come out with a conspiracy theory about great-power politicking, it will be even harder to sneer.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Italy's high-speed train link

Boring through the Alps

Dec 14th 2005 | ROME
From The Economist print edition

Demonstrators against a railway line also detect a conflict of interest

AFP

Stop, they say

THIS week, Italy's prime minister, Silvio Berlusconi, moved to calm a dispute over a rail tunnel through the Alps between Lyons and Turin. The 53-kilometre (33-mile) tunnel is a crucial link in a high-speed train line that is being built between eastern Europe and Spain. But after six weeks of clashes between protesters and the police, Mr Berlusconi has postponed the start of the work until another assessment is made of the project's environmental and health implications.

This is more than just a local tiff, and not just because the high-speed line crosses Europe. On the Italian side, it also runs through an area that is to be used for next February's winter Olympics in Turin. There were fears that the row might continue into and affect the games.

The tunnel's opponents are alarmed about its impact on an area of outstanding natural beauty. They say that the nearby mountains contain both asbestos and uranium, which they fear will be drilled out and left to blow around. With the support of some transport experts, they are also sceptical of the arguments for the line, and particularly of claims that it will sharply reduce truck traffic through the Alps.

But there is another reason why the row over the tunnel has become so bitter. Many protesters believe that Italy's infrastructure minister, Pietro Lunardi, has a personal interest in the project. The minister vigorously denies such claims, and has even threatened to sue the leader of Italy's Green party for making them.

A former academic, Mr Lunardi is the founder of a Milan-based firm, Rocksoil, which has been hired for some of Italy's biggest civil-engineering projects. His links with the company have been a source of controversy ever since he joined Mr Berlusconi's centre-right government in 2001. Before being sworn in, he duly resigned from Rocksoil. Although not legally obliged to divest himself of his shares, he then transferred them to close relatives, including his daughter and his wife.

Two years later, a financial daily, *Milano Finanza*, reported that Rocksoil's accounts showed that it had won a contract, as part of the Lyons-Turin railway link, for an access tunnel on the French side of the border. The contract was awarded by a French concern that had itself been contracted by LTF, the company in charge of the project. LTF is owned 50/50 by the French and Italian state-owned rail-network operators.

After this report, Italy's Greens tabled a question in parliament to Mr Lunardi about Rocksoil's

involvement. They say it was never answered. Mr Lunardi's department says that, since the contract was a French one and was awarded before he became a minister, there was no conflict of interest. There was thus no need to answer the question.

As it happens, a year later LTF announced that it was “constrained to cancel its contract with the group of companies entrusted with carrying out the work [on the access tunnel]”. A new consortium has now been appointed, though it is not clear if Rocksoil will carry out some of the work. But the protests over the tunnel will doubtless continue in any event.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Belarus

Turning the screw

Dec 14th 2005 | VILNIUS
From The Economist print edition

A benighted land darkens further

Get article background

LIFE is bleak for beleaguered democrats in Belarus. The country's autocrat, Alexander Lukashenka, has put tight controls on the media, rigged elections, torn up the constitution and sent opposition activists to jail, exile, or—as many fear of four of them who have disappeared—the grave. Now a new law on public security will make it a criminal offence to "discredit Belarus's standing abroad". If foreign-financed organisations, or the media, are involved, the penalty can be up to five years in jail. Training people to take part in street protests gets two years.

Against this background, the opposition is backing Alexander Milinkevic, a physicist, as a joint candidate in the election due next year. He has had a warm reception abroad—most recently at a meeting in Ukraine of a new pro-western block of ex-communist states. But that it is not what really matters. Wowing the salons of Brussels (where Mr Milinkevic is going next month) is far easier than electioneering at home, where official harassment is crippling his campaign. The independent media, although nominally free, must overcome big bureaucratic obstacles. The opposition has made the 16th of every month an occasion for public protest. So far, numbers taking part have grown each time. But with the police now allowed to shoot demonstrators, it would be understandable if numbers fell. Many Belarussians have given up on politics, and are concentrating on making money. The economy is booming.

The only channel of information that the government does not control is the internet—and even that may change. Local geeks claim that the authorities have bought software from China to block opposition-related content in e-mails or websites. Parliament is debating a new internet law which may impose further restrictions. Mr Lukashenka lavished compliments on China on a visit last week; his hosts reciprocated with a loan.

That may give Belarus more room for manoeuvre with its big patron, Russia. President Vladimir Putin loathes his bumptious Belarussian counterpart, but seems to have given up hope of dislodging him—though some think a Russian-backed putsch is possible.

The opposition and its western friends hope for a Ukraine-style revolution in Belarus. It could be a long wait.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Charlemagne

A modest proposal

Dec 14th 2005
From The Economist print edition

It is time to rethink the entire European Union budget

WHAT on earth is the European Union budget for? It is too small (taking up just over 1% of EU-wide GDP) to have any serious economic effect. To judge by the wrangling before this week's EU summit in Brussels, it has become mostly an opportunity for countries to air their pet grievances and to demand their money back. If there is a deal on the budget this week, it will be an agreement reached for its own sake, because EU leaders cannot bear to be blamed for yet another summit failure. And if there is no deal, it will similarly be a disagreement for its own sake—because France rather likes the idea of putting Britain, which holds the rotating EU presidency, in the dock for one more financial fiasco.

Yet if there was ever a good moment to think hard about how the budget might be better designed to advance the Union's stated aims, it ought to be now. The “financial perspective” is negotiated once every six years. That ought to create enough time to step back a bit and consider some first principles. The present negotiation is also the first since French and Dutch voters rejected the EU constitution in the summer, creating another good opportunity to ask whether the club is still spending its money on the right things. What would a budget look like if it took the EU's goals at all seriously?

The answer would presumably start by considering some of the things that might advance the cause of “ever closer union” (the preamble to the Treaty of Rome) as well as others that might promote growth and stability (once again, these are formal EU aims). A case could be made for some regional aid, on the ground that it advances ever closer union by helping to narrow the differences in income and infrastructure around Europe. Over one-third of the budget goes on such regional aid, so this bit at least passes one test.

The EU may, for this reason, be right to try to smooth out differences between countries—although there have also been several studies that query how effective its regional funds have actually been in practice. But the case for its intervening within countries is much weaker. That would surely be better done by national governments, which are likely to have greater knowledge of which regions and which projects merit support. Yet the EU gives help both to the poorest ("objective 1") areas of the Union and, even within rich countries, to their poorer regions. This second form of help (to objectives 2, 3 and 4, in the jargon) offends against the Union's principle of subsidiarity, which lays down that public intervention should take place at the lowest appropriate level of government.

As it happens, the EU has not shown itself to be particularly good at equalising income between countries, either. The two biggest net recipients of EU cash per head are Belgium and Luxembourg (because of the EU institutions located there). One of Europe's richest countries, Ireland, comes out above all but two of the new member countries from central and eastern Europe in net receipts per head. It seems equally perverse that Greece should get twice as much money per head as does Cyprus, or that Slovenia, the richest of the new members, should get more than Poland.

The principle of subsidiarity, as well as the aim of fostering economic growth, can sometimes justify financing things at European rather than national level. But the list is quite short. It might include the European Commission itself, as policeman of the single market; a few pan-European transport projects; common border controls; research that tends often to underfunded nationally (many Europeans consider that America's generous federal spending on research helps to give its economy a competitive edge); and, perhaps, some foreign aid (a single EU aid budget could avoid much of the duplication that confronts recipients of European aid, although the EU aid programme has often been criticised for being ineffectively delivered). As some of these items are now national, a sensible EU budget might even be bigger in certain areas.

Shrinking Brussels

But it would be a lot smaller in others. For what such a budget would certainly not include is the largest single item of current spending, agriculture, whose share of the total will actually rise, under the British presidency's compromise plans, from around 40% now to almost 45%. The common agricultural policy (CAP) is hard to justify on any "European" grounds. It does not contribute to economic growth. And, although one of the original bargains underlying the European project was that France would open its market to German exports in return for German taxpayers subsidising French farmers, the CAP today offers almost nothing towards the goal of ever closer union.

Moreover, the CAP also offends against the principle of subsidiarity. Most Europeans would be better off if there were no farm support at all. But if there is to be some, it should surely be doled out nationally, because only national governments have the expertise (and the political authority) to run what has increasingly turned into a personal income-support system for one particular interest group. Indeed, as the past few weeks have shown once again, CAP spending is not only divisive but has also helped to turn the entire EU budget into what the 2003 Sapir report, "An Agenda for a Growing Europe", memorably termed "a historical relic".

There is no question that the EU budget is broken, whether or not member countries manage to reach a deal at this week's summit. There is equally no question that a more rational budget would require huge changes in the pattern of spending and in the sources of finance. The Sapir report urged radical reform, but true to form the European Commission took the report, said thank you, and put it in the back of the drawer with the best linen, never to be used. Shame.

The police

Boys in blue

Dec 14th 2005
From The Economist print edition

Reuters

Britain's police, by repute the world's best, are unpopular at home

Get article background

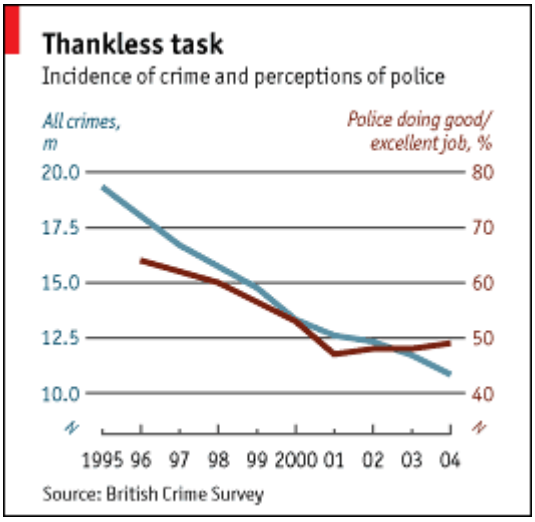
A POLICE officer on foot patrol in a touristy part of London is liable, sooner or later, to be asked to pose for a photograph. The distinctive teat-shaped helmet is part of the appeal; so is the British bobby's foreign reputation—reinforced by television dramas and detective fiction—for probity and incorruptibility. But, these days, the police are more popular with visitors than with the natives. At home, they have rarely been so beleaguered.

The coppers' job, as they see it, is to fight crime. At this they seem to be succeeding. According to the British Crime Survey, which is the most accurate way of measuring long-term trends, there was less crime last year than at any point since 1981. The fall has been particularly steep since the mid-1990s. In the past ten years, burglary and car crime have both declined by 57%, vandalism by 24% and assault by 49%.

But success appears not to suit the police. Even before the fatal shooting on July 22nd of Jean Charles de Menezes, a Brazilian electrician who was mistaken for a suicide bomber, they were falling from favour. MORI, a pollster, found this spring that just 58% of people trusted them to tell the truth—a record low. Since 1996, the proportion of people who told the British Crime Survey that the police were doing a good or excellent job has fallen from 64% to 49% (see chart).

Martin Innes, a Surrey University sociologist, says that the more people have to do with the police, the less they seem to think of them. Whereas most Britons take a dim view of the National Health Service but are pleasantly surprised when they have to use it, the opposite holds

true for the police and the courts. Three years ago, a Home Office survey found that, whereas 31% of the general public thought the criminal justice system was effective in reducing crime, only 25% of victims (and, perhaps more significantly, just 23% of people who had been in the dock) agreed.



Attitudes are hardening even among the police's natural allies. Edward Garnier, Conservative MP for Harborough, an affluent East Midlands seat, says that “people who live in large houses, up long drives” have become much more critical in recent years. The reduced threat from crime may have something to do with this. When crime is rampant, the well-to-do see coppers as a bulwark against disorder. When it is low, they come to associate the police with speeding tickets.

Perhaps sensing the change of mood, Conservative politicians are talking tough. When the party was in power during the 1980s and 1990s, it was reluctant to entertain any criticism of the police. But the Tories' new leader, David Cameron, talks about “the last great unreformed public service”. The party wants a bonfire of government targets and red tape, which the police support. Coppers are less keen on Tory proposals to bring them under local democratic control—a demand that used to be associated with the extreme left.

Radical policies are required, says Nick Herbert, who speaks for the party on police reform, because the police have been drawn so closely into the government's embrace. Tories were enraged when, last month, police officers ran a co-ordinated campaign to bend MPs' ears over a government bill that would have given them the right to hold suspected terrorists without charge for 90 days.

The police have, indeed, enjoyed generous funding and influence over lawmaking in recent years. When Tony Blair was the youthful opposition spokesman on home affairs, he canvassed police chiefs on the powers and reforms they wanted. Since 1997, Labour has given the police most of what they desire, plus some powers they would rather do without. Earlier this month, a senior police officer declared that Mr Blair's proposal to allow the police to shut down places of worship associated with extremism would send “the wrong message” to Muslims, and make the police's job more difficult.

Too much power turns out to be bad for the police. In October, an anti-war demonstrator who tried to hold an unofficial remembrance service for the Iraq war dead was arrested under a new law that bans impromptu protest in Westminster. The demonstrator was found guilty, which suggests that the police had in fact interpreted their powers correctly. But that was not enough to silence critics. “Sometimes, you wonder whether the police have taken leave of their senses,” wrote one commentator in the *Daily Telegraph,* a newspaper that normally bangs the drum for law and order.

A surfeit of power also makes the police vulnerable to the opposite accusation: that they are not doing their utmost to tackle crime. Coppers used to claim, with some justification, that their attempts to clean up the streets were hampered by inefficient courts and liberal magistrates. But many of Labour's criminal-justice innovations, such as penalty notices for misbehaviour, deliberately bypass the courts and hand power directly to the police. That removes their traditional excuse.

“There is an expectation that, as soon as a power becomes available, we will use it,” says Peter

Neyroud, chief constable of Thames Valley police. But the sheer volume of criminal justice legislation leaves the police bewildered, and actually makes learning new tricks more difficult.

Coppers such as Mr Neyroud and Sir Ian Blair, commissioner of the Metropolitan Police, are now pinning their hopes on a return to an old-fashioned way of doing things. Neighbourhood policing schemes, which are mushrooming across the country, seek to bind officers to a local beat and get ordinary people involved in setting police priorities. Such schemes look rather like the watchmen and ward constables that existed in the early 19th century. Those figures were swept away in the name of efficiency. These days, though, the police might be willing to trade a little efficiency for a bit more popularity.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Politics

Lib Dem rumblings

Dec 14th 2005
From The Economist print edition

Charles Kennedy's leadership is under threat

Get article background

POLITICS being the zero-sum game that it is, the emergence of David Cameron as a new Tory leader determined to re-occupy the centre ground of British politics was bound to have repercussions elsewhere. One of the main casualties could be Charles Kennedy, leader of the Liberal Democrats.

Long-running rumblings of dissatisfaction with Mr Kennedy now appear to have come to a head. This week, at a meeting of the Lib Dems' shadow cabinet, senior colleagues told Mr Kennedy to shape up or ship out.

It is not the first time this has happened. Last year, he was told to raise his game and attend to his suspect health (a euphemism for Mr Kennedy's enjoyment of a tipple). Up to a point, he did. But his performance during the election in May was seen as lacklustre and the party failed to win more than a handful of seats against unpopular opponents.

Since then, frustration with Mr Kennedy's lack of cutting edge and failure to give stronger backing to policy modernisers has grown. Now there are fears that Mr Cameron will steal Lib Dem clothes on social and green issues.

The one thing that might still save Mr Kennedy, however, is the lack of an obvious replacement. The party's 62 MPs have little time for the activists' favourite, Simon Hughes. They would almost certainly prefer Sir Menzies Campbell, their distinguished foreign-affairs spokesman, as a caretaker leader until the next election. But the 64-year-old Sir Menzies is 18 years older than Mr Kennedy and was ill in 2003. Much may depend on his appetite for taking on the 39-year-old Mr Cameron.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Evidence under torture

The fruit of the poisoned tree

Dec 14th 2005
From The Economist print edition

When evidence obtained by torture can and cannot be used

THE law lords were at their most majestic last week, and their unequivocal condemnation of the use of evidence obtained by torture reverberated around the world. “The English common law has regarded torture and its fruits with abhorrence for over 500 years,” Lord Bingham thundered: “I am startled, even a little dismayed, at the suggestion...that this deeply rooted tradition and an international obligation solemnly and explicitly undertaken can be overridden by a statute...” In short, secret evidence which might have been obtained by foreign governments through torture cannot be used against terror suspects in British courts. And it is up to the British government to prove that such information is not tainted in this way.

The ruling springs from an appeal against deportation by ten suspects detained under Britain's anti-terrorist laws. It clears up—or seems to—ambiguity surrounding the prohibition on the use of evidence secured through torture that is enshrined in the UN Convention Against Torture. Britain and the other 140 parties to the treaty must ensure that “any statement which is established to have been made as a result of torture shall not be invoked as evidence in any proceedings...”

Some have argued, however, that this prohibition does not necessarily extend to evidence provided by other governments or third parties. Charles Clarke, Britain's home secretary, maintained that the ban applied only when the state in whose jurisdiction the proceedings were held had itself inflicted or been complicit in torture. Few courts in other countries have ruled on the matter, but those that have—in France, Canada, Germany and the Netherlands, for example—held that evidence obtained by torture is always inadmissible.

Britain's House of Lords is now the most important court in the world so to rule. Nothing could be clearer, surely, than its message? Yet the decision is not easy to interpret nor its impact to predict.

The ruling is certainly not the sock in the eye for the government that some human-rights activists are claiming. Ministers have insisted all along that the government “does not present to court evidence that is believed to have been obtained by torture”. And the law lords did not ban the use of tainted evidence in executive decisions, such as those on deportation and control orders, though the ruling would apply if the decisions were appealed. The government is relying increasingly on such measures rather than on criminal trials in its fight against terrorism.

There is another reason, too, why the ruling may not have the impact that some expect. If the appellant can produce a “plausible reason” why evidence may be tainted, the burden of proving that it is not shifts to the government—but the required standard of proof is not of the highest. On this, the seven-judge panel was unanimous. But three of the law lords, led by Lord Bingham, argued that the evidence should not be admitted unless the government could show that there was “no real risk” that it was based on torture. The other four ruled that the government should have to show only “on the balance of probabilities” that the evidence was clean. If doubt remained, the court should admit the evidence but bear that doubt in mind when evaluating the

evidence.

For all its nuances, the law lords' ruling is a landmark. It is bound to have repercussions elsewhere—including America. The Supreme Court of the United States has never been asked to pronounce on the matter. But, in 1974, the federal First Circuit Court of Appeal ruled that it was “unthinkable that a statement obtained by torture...should be admitted at the government's behest in order to bolster its case”.

In a sly aside to last week's decision that has left the Bush administration fuming, Lord Hoffmann wrote that “many people in the United States, heirs' to [Britain's] common-law tradition, have felt their country dishonoured by its use of torture outside the jurisdiction and its practice of extra-legal ‘renditio’n of suspects to countries where they would be tortured.” America's secretary of state, Condoleezza Rice, insists that her country “does not permit, tolerate or condone torture under any circumstances”. But suspicions remain that secret CIA interrogation centres for terrorist suspects do exist in Europe and elsewhere. The law lords' ruling is seen by many as a sharp rebuke.

What will its impact be in Britain? Some commentators have suggested that as many as 30 terrorist suspects could now be released from detention or control orders as a result of the ruling. But one of the judges, Lord Brown, wrote that it “seems unlikely that the exclusionary rule...will affect many, if any, individual cases”. Mr Clarke, too, insists that the ruling will not “change, weaken or detract from our ability to fight terrorism”. But it could make the government a little warier about where it gets its information.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

School reform

Sorting out schools

Dec 14th 2005
From The Economist print edition

What happens when parents choose

Get article background

PARENTS have done the legwork and sent in the applications. Now they face an anxious wait until the spring, when they will hear whether their children are among the lucky ones who are offered places at their chosen schools. In the meantime, they will have to listen to hair-raising tales of children turned down by every school they applied to, and of schools with 20 applications for every place that are so popular they only accept those who live within a five-minute walk.

Earlier this month, a government-commissioned poll found that more than a third of parents felt the choice of secondary schools in their area was “poor”—ten percentage points more than just a year ago. And they are increasingly willing to act on their worries. Many will move house to get nearer to the school they want, or even resort to more underhand methods—a 2004 poll found that more than a quarter of parents would consider lying about their address or religion to get their child into the school they prefer.

So October's education white paper caught the mood with its subtitle: “More choice for parents and pupils”. It sets out a vision of “independent state schools” managing their own admissions and finances, each with a distinctive ethos and a specialist subject, competing to attract parents and free to expand to meet demand. Private schools, including religious ones, will find it easier to move into the state sector, and failing schools will have to improve within a year or risk being closed or taken over.

These proposals are facing strong opposition from many Labour MPs, and on December 14th, a group of backbenchers presented an 11-page critique. One of their main worries is that giving schools more freedom over admissions will reintroduce academic selection on the sly—a fear that was cleverly heightened by the new Tory leader, David Cameron, who last week said the prime minister could rely on Tory support to force his bill through. There were signs this week that the government is beginning to backtrack.

The backbenchers have a point. A school's exam results are determined mainly by the ability of the students it admits and the attitudes of their parents—both of which are strongly linked to social class and income. School-level influences, such as good teachers and a strong head, have less effect. Since the white paper rules out overt selection by ability, the simplest way for a school to improve its results is to admit more children from well-off families. So the worry is that schools will use gerrymandered catchment areas and increasingly elaborate selection procedures to ensure a better-than-average intake. Since not every school can be above average, this would inevitably mean less popular schools getting more than their fair share of the difficult to teach.

Some of the worriers are nostalgic for a straightforward system of neighbourhood schooling, where children simply attend their local schools. It would be tidy and easy to administer, and pushy middle-class parents wouldn't be able to take advantage of labyrinthine admissions policies.

It would also end all hope of using market signals to drive up standards, which is presumably part of the attraction for some. And there is another snag: neighbourhoods themselves are often socially stratified. Sending all children to their local schools would increase housing segregation, because house prices near popular schools would go up until only the rich could live there. These effects can be very large: one analysis showed that houses right next to the most popular schools could command a premium of more than £60,000 ($105,000).

But research on the impact of choice in education carried out at the Centre for Market and Public Organisation, a think-tank, offers some cautious support for the policies in the white paper. It concludes that the greatest social sorting occurs when parents are free to choose but supply is rigid; next comes strict neighbourhood schooling; and the least takes place when parents choose and schools respond quickly to market signals—that is, when it is easy to set up new schools and expand popular ones, and unpopular schools quickly close.

In 2003, big increases in teachers' salaries and pension costs meant that some schools with falling rolls looked like getting less money than they had the year before. In the face of bad publicity, the government quickly re-jigged the funding formula to lessen the impact of changing student numbers—reducing the incentives for schools to expand. It is not a good omen: when choice starts to work, and the losers start to squeal, the government backs down.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

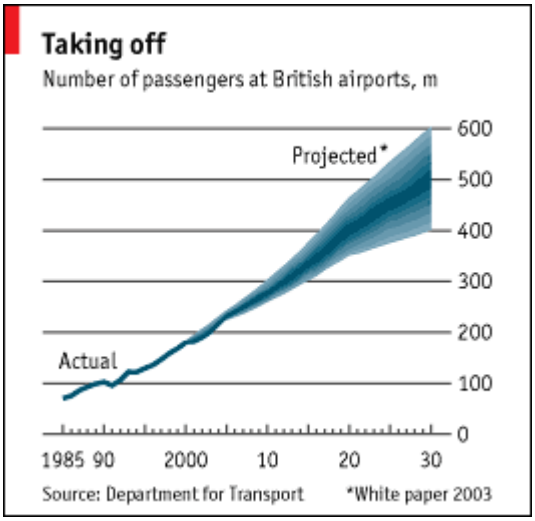
Economist.com WORLD EUROPE

Airports

Headwinds

Dec 14th 2005
From The Economist print edition

Plans to expand airports are causing headaches for the government



SINCE Labour came to power, it has mostly ducked the toughest question in transport—building new capacity. Looking at the rows over aviation, official timidity seems understandable. This is the one area of transport where lots of expansion is on the cards, for the number of passengers through Britain's airports is expected to rise from 215m a year today to 500m by 2030 (see chart). Bigger airports are clearly needed, but the subject is viciously controversial. And pressure is building for the sort of sensible tax and emissions policy that could reduce the increase in air passengers.

In 2003 ministers announced an ambitious programme of airport expansion, hinging on two new runways in the south-east—one at Stansted and, later, another at Heathrow. That decision caused a storm of protest when it was announced. It flared up again last week when BAA, the former state monopoly that controls all of Britain's big airports, announced its plans for the new runway at Stansted.

The condemnation was immediate and universal, despite the fact that the new proposals, at £2.7 billion, were £1 billion cheaper than the government's initial guess. Local residents worry that more flights will mean more noise, more congestion on the road and on railways and, potentially, the construction of thousands of new homes for workers at the new, expanded airport.

The airlines aren't pleased either. BAA has admitted that a new runway at Stansted will be economically viable only if it is cross-subsidised with money from Heathrow. Airlines that land at the bigger airport dislike the idea of coughing up for new capacity for their cut-rate rivals at Stansted. The airlines based at Stansted—especially easyJet and Ryanair—think that BAA's plans are grandiose and too expensive. They say the higher landing charges needed to pay for the expansion will scare away passengers.

It may seem odd that the Stansted argument is taking place at all, given that the airline industry would prefer to see Heathrow expanded first. But pollution around Heathrow is now so bad that it will breach European guidelines due by 2010. The government has said that no new runway will be built there until air quality improves, although cynics point out that Heathrow's history is one of broken promises, and that greenery has always lost out to growth.

In the meantime, BAA and the government are doing their best to squeeze as much as possible out of Heathrow's existing capacity. In June, the Department for Transport (DfT) proposed increasing the number of night flights from 5,800 a year to 6,420. Next year it will suggest using both existing runways for takeoffs and landings, thus permitting even more flights. That provoked

howls from long-suffering locals, who say that noise pollution from Heathrow hurts house prices, causes stress and makes it impossible for their children to concentrate at school.

The broadest criticism comes from green groups, who say that the government's entire policy is misguided. Compared with most other forms of transport, they maintain, aviation is under-taxed. Airlines pay no fuel duty, and passengers pay no VAT. These tax breaks inflate demand. In 2003, Friends of the Earth, an environmental pressure group, asked the DfT to re-run its computer models, assuming that aviation fuel was taxed at the same rate as petrol and that the VAT exemption was removed. Passenger numbers predicted for 2030 fell to 315m, 37% below the government's estimate. So much of the planned new capacity would go unused.

This is a particularly stinging criticism for a government that prides itself on its commitment to tackling climate change. Greenhouse gas emissions from aircraft are rising rapidly. By 2030 aviation is expected to account for a quarter of Britain's total greenhouse emissions, up from around 5% today.

In its defence, the government points out that kerosene taxes are set internationally, and that taxing the fuel unilaterally would in any case be futile. Instead, ministers want to push for the inclusion of aviation in the second round of the European Emissions Trading Scheme, which starts in 2008. But timetables have slipped, and there is now concern that the government will prove unable to meet its deadline.

Taxing transport is always politically sensitive, as Labour discovered when it provoked protests over fuel prices in 2000. Tony Blair is acutely aware of the dangers: speaking before the election, he ruled out “some huge tax on cheap air travel”. But transport policy is full of difficult decisions, and on aviation, at least, the government has already taken several. It would be a shame if it could not muster the courage for one more.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD EUROPE

Ranking public services

Made to measure

Dec 15th 2005
From The Economist print edition

But Britain's performance is hardly bespoke

BRITAIN'S public services may not be “world-class”—the stated ambition of the Labour government—but they are world-beaters in one respect. From star ratings for hospitals to league tables for schools, performance measurement reigns. Targets abound and inspectors proliferate in Britain's audit culture.

The ranking business encompasses local councils, even though they are supposed to answer to voters. Every year, the Audit Commission, an official watchdog, judges how they are doing in England. On December 15th, it issued its latest “comprehensive performance assessment” (CPA).

This hotel-style measure ranks councils by stars, ranging from four to none. A score of two stars is the minimum that should be achieved. The ratings take into account how councils perform on a range of services, such as those for the local environment; use of resources, including value for money; and general strategy and management.

Two-thirds of councils win overall rankings of three or four stars, according to the new CPA. On value for money, the record is less satisfactory, with just over half scoring that high, and few among them getting four stars. In the overall rankings, ten of the 150 councils are performing very badly, achieving one or no stars.

But does any of this actually lead to better public services? The commission claims that CPAs have helped to drive improvement since they were introduced in 2002, so much so that it has had to make the test harder this year. However, Simon Milton, the leader of Westminster City Council, a four-star authority, describes the CPA as a “game” that “risks becoming a meaningless process-driven exercise”.

Certainly, there is little evidence that Britain's obsession with performance assessment, which pre-dated the Labour government of the past eight years, has done much for its public services compared with other countries. Earlier in the week, Christopher Hood of Oxford University told a conference on international public-service rankings that Britain came 11th out of 13 rich countries over the period 1990-2005. Naturally, Labour says it has made a difference since it won power in 1997. But the rankings show little change in Britain's performance over the past decade, according to Mr Hood.

Findings like this will not hold back Britain's measurement-mad government. Next in line is Whitehall, as ministries have to submit to “departmental capability reviews”. But worry not, Sir Humphrey. Sensibly, the top mandarins are planning to keep the exercise in-house without the bother of external assessment by a watchdog like the Audit Commission. The real thing is fine for weak local councils but lacks appeal for those at the centre who hold power.

Economist.com WORLD EUROPE

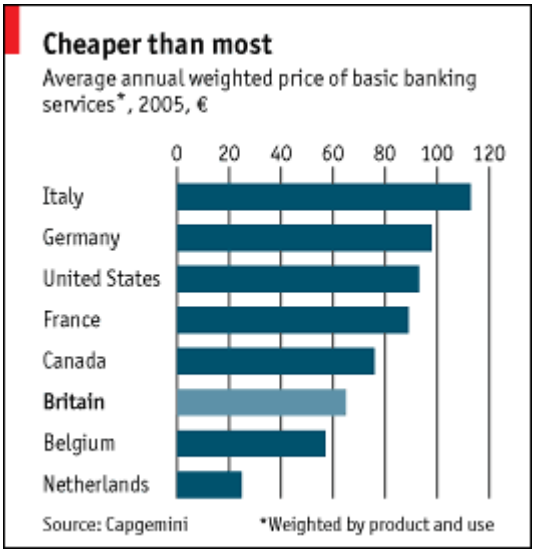
Banking competition

Another day, another probe

Dec 14th 2005
From The Economist print edition

Allegations of market failure plague banks in their most profitable year ever

FOR an industry that likes to think of itself as staid and grey-suited, Britain's banks have been getting far more attention than they would like. Last week the Office of Fair Trading (OFT), a competition watchdog, said that it planned to scrutinise the market for payment-protection insurance on loans, valued at £5.4 billion in 2003. Profit margins on loan-insurance policies appeared high, the regulator said. Just a month earlier, the Financial Services Authority (FSA), the industry's main regulator, said that investigators who went undercover to check into the matter found firms at risk of mis-selling these policies.



The OFT probe is just the latest in a long line of recent inquiries into British retail banking. The Competition Commission, another watchdog, has three investigations in progress. Other British regulators and a parliamentary committee have another ten or so in the works.

In fact, bank customers in Britain pay less overall than those in many comparable economies. As the chart shows, the average British consumer spends €65 (£44) a year on banking services, according to a 2005 study by Capgemini, a consulting firm. That compares with €113 in Italy, €98 in Germany and €93 in the United States.

Yet for all the rivalry between the country's banks, which include three of the world's ten largest, there is a disquieting lack of competition in some areas of the market. Lenders compete fiercely to make mortgage loans; and a review that David Miles, an academic, carried out at the government's behest said last year that the mortgage market was generally working well. But the same level of competition is not evident across all financial products. Several OFT studies have found restricted competition in store-branded payment cards, doorstep loans and credit-card transaction fees, for example.

This suggests that there has been relatively little change since 2000, when a government-appointed review headed by Don Cruikshank, formerly director general of Oftel, the telecommunications regulator, found market failure in the provision of banking services to consumers and small businesses.

“The government has a problem with the banking industry,” said David Lascelles, a director of the London-based Centre for the Study of Financial Innovation, a think-tank. “To some extent that problem is legitimate. There is a surprisingly small amount of competition.” Observers posit two contrary explanations for this: too much regulation and too little.

In an industry such as banking where there are high barriers to entry, adding rules simply makes it more difficult and expensive for new entrants to compete. It can also carry unintended consequences, as the Competition Commission found not long ago.

A two-year study into banking for small businesses, completed in 2002, found that weak competition was allowing big banks to charge excessive fees. The government ordered them either to provide free services to small businesses or to pay interest on their current accounts.

But the remedy may have compounded the illness. Abbey National and Alliance & Leicester, Britain's sixth- and eighth-largest banks, complained that the regulator's intervention in fact stunted their growth.

While the big banks were merrily whacking their small business customers over the head, their smaller rivals had been tempting clients with offers of free banking or interest-bearing accounts. When bigger banks were required to do the same, customers had less incentive to switch and, arguably, competitive forces in the market were reduced. The OFT plans to review the measures next year.

But there is also merit in the argument that more regulation can help to boost competition. Sir Callum McCarthy, chairman of the FSA, argued in a speech last month that to achieve competitive markets regulators must make detailed rules compelling firms to provide information to their retail customers. Only then can consumers make informed choices.

This, broadly, is the approach that regulators are now following. In the past year, they have made banks explain more clearly the interest rates they charge on credit-card debt and the fees for withdrawals from cash machines.

For transparency to succeed, however, consumers must exercise their power. Sadly, they cannot always be relied upon to do this. At least 75% of customers have never switched banks, according to figures from MORI, a polling firm.

Perhaps, however, this should not come as a surprise. According to the FSA, a fifth of all bank customers don't understand percentages.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Bagehot

The good European

Dec 14th 2005
From The Economist print edition

Is Tony Blair's European policy in tatters? Not really

Get article background

IN OCTOBER 1997, soon after Labour's landslide election victory, Britain's most prominent pro-European, Roy Jenkins, advised the young prime minister that he had a chance to “seize the moment” and to shape events rather than be shaped by them. The choice for Tony Blair, as Lord Jenkins saw it, was between leading in Europe, which would require joining the nascent euro, and keeping the Rupert Murdoch-owned press on his side.

Typically, Mr Blair declined to see things so starkly. Although he had described securing membership of the single currency as one of the most important decisions facing the country, he calculated that a lot more needed to be done to prepare the ground politically and economically before the promised referendum could be won. And what was the point of making an enemy out of Mr Murdoch when he had worked so hard to woo him?

As Lord Jenkins had predicted, the moment passed. For ardent Europhiles, who had believed that Mr Blair, in his own words, would finally end Britain's historic ambivalence towards Europe, it was never glad confident morning again. As far as the Eurosceptics were concerned, nothing Mr Blair did or didn't do would convince them that he wasn't a fanatical integrationist straining at the leash to do the bidding of “Brussels”.

As Mr Blair struggles to find a resolution to the European Union's budget crisis—when *The*

Economist went to press, the prospects were in the balance—he knows that whatever the outcome, he can expect blame rather than praise. By putting even a small part of the British rebate on the table without having previously secured root-and-branch reform of the common agricultural policy (CAP), he already stands accused by the predominantly anti-European British press of having betrayed Margaret Thatcher's great victory more than 20 years ago in Fontainebleau.

If, on the other hand, despite Mr Blair's willingness to offer something for very little in return, there is no deal, it will be he, not the real villain of the piece, Jacques Chirac, who will get it in the neck from the other 24 member countries. The one thing that almost everyone is agreed on is that Britain's six months presidency of the council has been dismal—a fitting culmination to Mr Blair's European policy of the past eight and a half years.

One does not have to be an apologist for Mr Blair to see this as an excessively harsh verdict. A large part of the problem with Tony Blair in Europe, as it is at home, is that he raises the bar of expectation too high. Just as he led euro-enthusiasts to believe he would do something that he must have known neither the Treasury nor the British public would let him, so his rousing speech to the European Parliament in June was almost bound to result in anti-climax and disappointment.

As a passionate exposition of how a more open and economically dynamic Europe would better serve the interests of its citizens, it could not be faulted. But the idea that Britain, of all countries, in a six-month period interrupted by summer holidays, could persuade the French effectively to abandon the CAP deal (that runs until 2013) stitched up with the Germans three years ago was wildly over-optimistic.

The notion that Mr Blair's European policy has been a flop is equally daft. With a clear sense of direction, diligence and charm (good luck also played a part when the European constitution was derailed), he has transformed Britain's position in Europe. The much-derided British presidency succeeded in salvaging the EU's faltering commitment to beginning formal entry negotiations with Turkey—something of great strategic importance that possibly no other country could or would have done.

Above all, the long-term British strategy of enlarging the Union at the expense of further integration has been a triumph for patience and persistence. While the budget wrangling has temporarily strained relations with the new eastern European members, they know that no major country has done more to bring them into the Union or extend to them the full rights of membership than Blair's Britain. The idea of France and Germany as the motor of an ever-deepening union has been dealt a lasting blow. France's rejection of the European constitution was a cry of pain against the Europe that Mr Blair has helped to construct.

Bolstered by its own economic self-confidence, Britain has also had some limited success in gaining support for a more liberal, more competitive union. It's true that progress on the ground since the Lisbon summit in 2000 is hard to discern, but the new commission, headed by José Manuel Barroso, is far more in tune with the British agenda than any of its predecessors. It is a reflection of the new balance of power in the EU.

Still ambivalent after all these years

Compared with the catastrophic state of affairs that developed under the last Conservative government, symbolised by John Major's pathetic “empty chair” response to the ban on BSE-infected British beef exports, Labour ministers work effectively with their European counterparts and get results. Any moment now, Charles Clarke, the home secretary, is expected to announce a Europe-wide agreement to retain mobile phone data that may help to trap terrorists.

Even Mr Blair's “failures” no longer look so bad. As the gilt wears off the euro, Britain's reluctance to sign up seems slightly less offensively idiosyncratic to the currency's boosters. Meanwhile the diplomatic damage done by the Iraq war has been partially healed by the decline in the fortunes of Mr Chirac and Gerhard Schröder and the need to rebuild transatlantic bridges.

Mr Blair may have been no more successful in ending Britain's ambivalence to Europe than in teaching the Labour Party to love Peter Mandelson. Some things are impossible. But what he has done is to advance Britain's interests by engaging with Europe calmly and constructively. When the brickbats start flying this weekend, as they will, that's worth remembering.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

India

The next wave

Dec 14th 2005 | DELHI
From The Economist print edition

India's IT and remote-service industries just keep on growing

ASKED for a sound-check at a function in Delhi this month, Bill Gates eschewed the "1,2,3..." favoured by ordinary mortals. "One billion, 2 billion...," he counted. They think big, these IT moguls, and especially, these days, in India.

Microsoft later announced plans to invest $1.7 billion in India over the next four years, about half of it in adding to its existing research and development (R&D) and technical-support operations. "The only thing that limits us in India," Mr Gates told the local press, "is the speed at which we can recruit." A few days earlier, Intel, a giant chipmaker, had unveiled plans to invest more than $1 billion over five years, much of it in expanding its R&D centre in Bangalore. In October Cisco Systems, the world's largest maker of the routers and switches that direct internet traffic, announced its own plans to invest $1.1 billion in India.

The euphoria is confined neither to American multinationals, nor to information technology. It also encompasses India's own IT industries, and the expanding range of other back-office services that can now be performed remotely. The three biggest Indian IT-services firms—Tata Consultancy Services (TCS), Infosys and Wipro—are each recruiting more than 1,000 people a month. And to take just one example of the other services now moving to India, J.P. Morgan Chase, a big investment bank, this month revealed it is to double, to about 9,000, its staff there. Anyone who assumes J.P. Morgan will simply be doing low-level "back office" tasks in the country—a bit of data entry and paper-shuffling—would be flat wrong. One task for the new recruits is to settle complex structured-finance and derivative deals, what one insider calls "some of the most sophisticated transactions in the world".

All these investments illustrate that a third stage of the great Indian services-export boom is well underway. In the first, firms such as TCS developed world-class expertise in software “application development and maintenance”, and their low-cost developers became the preferred partners of many Western IT firms. In the second, Indian firms and the local “captive” operations of multinationals started offering low-end back-office services that could take place a continent away—telephone call-centres, transcribing medical records, processing insurance claims and so on. In the third, in both IT and the broader spectrum of other “business processes”, ever-more sophisticated functions are happening in India.

So strong are the forces driving this shift that what seemed improbably rosy projections by NASSCOM, the Indian software- and service-industry lobby, and McKinsey, a consultancy, back in 1999, are coming true. This week NASSCOM and McKinsey produced the second full-scale update of their study. It argues that exports from India's IT industry and from “Business Process Offshoring” (BPO)—both from services “outsourced” to Indian firms and those performed by captives—are on track to reach $60 billion a year by 2010.

That would be a huge surge from the $17.2 billion in the year ending in March 2005. But it implies a compounded annual growth rate of 28%—below that achieved in recent years. Moreover, according to McKinsey's estimates, it requires India merely to maintain its present shares of the markets for offshore IT services (65%) and BPO (46%). This is because the study predicts a massive rise in the size of the overall market, estimated at present to make up just one-tenth of those services that could be sent offshore. The proportion is expected to rise as demography—a western labour shortage—becomes more pressing than protectionism.

In IT the growth in Indian exports is expected to come both from the software market, and from “traditional IT outsourcing”—such as the remote management of whole systems, a market now dominated by the big global IT consultancies. This is expected to rise from 8% of Indian sales now to about 30% in 2010, while software-development's share will fall from 55% to 39%. In business-process-offshoring, the big industries will remain banking and insurance. But rapid expansion is also expected in other areas, like legal services.

The law, in fact, illustrates how vast is the untapped potential market. About $250 billion is spent on legal services world-wide, about two-thirds of it in America, and as yet only a tiny proportion goes offshore. Forrester, a research outfit, has estimated that, by last year, 12,000 legal jobs had moved offshore, and forecast that this will increase to 35,000 by 2010. India, with its English-language skills and common-law tradition is well-placed to secure a big share of the business. It is not just a question of “paralegal” hack work such as document-preparation. Sanjay Kamlani, of Pangea3, a small Indian firm, calls it “real lawyering”—drafting contracts and patent applications, research and negotiation. His clients are both big law firms and in-house legal teams.

India's fundamental attraction has not changed since it first drew software developers: fantastic cost savings. With American lawyers costing $300 an hour or more, Indian firms can cut bills by 75%. Across the board, despite climbing rates of pay in IT and BPO, where rapid expansion has brought frantic job-hopping, India remains, say NASSCOM and McKinsey, the lowest-cost of all the main outsourcing destinations. It also has, among these countries, by far, the largest pool of employable people—those with the necessary language and technical skills. On this measure, India, which produces 2.5m graduates a year, 250,000 of whom are engineers, has 28% of the global available workforce, compared with 11% in China.

Yet the supply of talent may be the biggest constraint on the Indian industry's growth. On these latest projections, the number of people working in IT and business-process exports in India will increase from about 700,000 now to 2.3m by 2010. But on today's estimates only 1.05m suitably qualified people will graduate from college between now and then, so there will be a shortfall of nearly 500,000, with business-processing the worst affected. McKinsey's Jayant Sinha believes the

education system can be fixed in time to plug the gap. A bigger worry, he says, is India's creaking urban infrastructure. IT firms in Bangalore, for example, are in revolt against the local government for its neglect of basic amenities. Yet India's IT and business-process industries will need about 14m square metres (150m square feet) of office space by 2010: “a new Manhattan”.

Hectic building is under way, and not just in the big IT and business-processing centres (Bangalore, Mumbai and around Delhi) or the “second tier” of cities such as Pune, Hyderabad and Chennai (Madras). The industry's worry over infrastructure, as over education, is that it cannot do everything by itself. Having thrived by keeping government at arm's length, business now needs help.

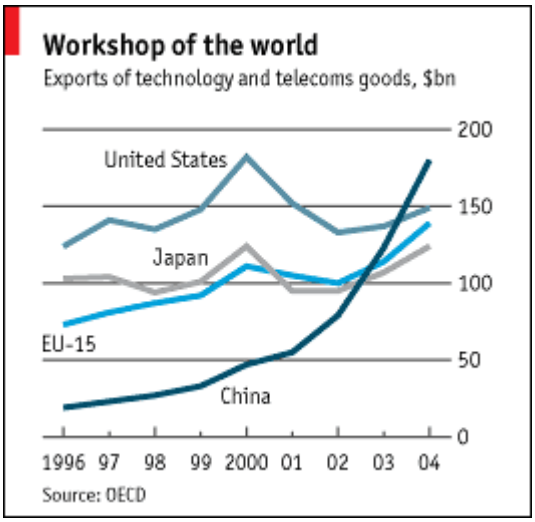
Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Information technology

Digital dragon

Dec 14th 2005
From The Economist print edition

China has replaced America as the world's largest exporter of IT goods



IN 2003, at the United Nation's World Summit on the Information Society, huge banner advertisements lining the streets of Geneva were emblazoned with the names of Nokia and Hewlett-Packard. This November, at the second phase of the summit in Tunis, the banners flagged the names of Huawei and ZTE, China's telecoms-equipment powerhouses, while the PCs at the event bore the brand name Great Wall.

This week the anecdote was backed up by numbers. China for the first time has surpassed America to export the most technology wares around the world, according to new figures from the Organisation for Economic Co-operation and Development. The crossover took place last year, when China exported $180 billion of computers, mobile phones and other digital stuff, exceeding America's international sales of $149 billion. A year earlier, in 2003, China's technology exports had overtaken those of both the European Union and Japan.

Given China's importance as a centre of low-cost manufacturing, its rise as an industrial power in technology goods is hardly surprising. What is startling is the speed of its ascent. From $36 billion in 1996, its world trade in tech goods—both imports and exports—has grown as much as 32% a year, to reach $329 billion in 2004.

China's rising share of the market has been matched by a fall in the dominance of America—which invented the electronic computer and transistor that launched the digital era. Almost all big IT firms have welded China into their supply chain. In that light, the sale of IBM's PC division to the Chinese computer-maker Lenovo, which made headlines a year ago this month, made perfect sense.

China is now the biggest IT exporter to America, having overtaken Japan in 2004. It accounts for 27% of all American IT imports (from 10% in 2000), which last year generated a trade surplus of $34 billion. For the moment, China's edge is in the low-end work: it imports components, fits them together and exports finished goods. But, after the second world war, Japan also started this way—before moving from low-wage labour to more advanced work, in many instances by capitalising on technological breakthroughs that came originally from America. China is also striving to imitate the Japanese model in another way, by working on its own technology for the next phase of development. But that is more an aspiration than a reality—at least for the moment.

Economist.com BUSINESS

Obesity and advertising

Junior fat

Dec 14th 2005
From The Economist print edition

Concern is growing over junk-food ads aimed at children

Digital Vision

Wasting his salad days

THERE is no doubt that advertising influences children—ask any parent. Some toddlers seem to be able to spot the golden arches of a McDonald's restaurant from a mile away. And they soon learn that a “Happy Meal” comes with a toy, often based on a popular cartoon character. But does such marketing also help cause childhood obesity? Recent reports in America and Europe have put the food industry on notice that unless the advertising of junk food to children is curbed, legislative action may follow.

The most damning criticism comes from America's Institute of Medicine (IOM). It reckons that most of the $10 billion or so spent last year on marketing food and drink to young Americans was for stuff that was high in calories and low in nutrients. This, it says, puts children's “long-term heath at risk”. Around 16% of American children aged 6-19 are now obese—three times the level of the 1960s.

If the food industry does not voluntarily start promoting more foods that are lower in calories, fat, salt and added sugars, then the IOM believes Congress should take action. One area it is particularly concerned about is the use of licensed film-characters, such as Shrek or Scooby-Doo, to promote junk food.

Officials in Europe are also worried. Last week the European Commission launched a public consultation to find ways to reduce obesity, which it says is increasing at an “alarming rate”. In Scotland, home of the deep-fried Mars bar, more than a third of 12-year-olds are overweight. The commission is exploring various ideas, among them persuading the food and advertising industries to restrict junk-food marketing voluntarily.

Some in the American food industry have reacted with alarm and likened the IOM study to the 1964 Surgeon General's report on smoking, which ultimately led to bans on tobacco advertising. They have criticised the fast-food report for not taking into account what has already been achieved—notably some 4,500 healthier food products launched in the past three years, according to the American Advertising Federation. It believes children would be better served by encouraging them to do a few press-ups, rather than by protecting them from advertisements. People are fat, says the federation, because of “a lack of strenuous physical activity”.

Nevertheless, some food companies are finding opportunities to sell healthier products. An emphasis on healthier eating and living has helped PepsiCo in its perennial battle against Coca-Cola (see article). And faced with declining sales even before Morgan Spurlock put the boot in with his film “Super Size Me”, McDonald's has been overhauling its menu. Sales of salads, fruit, bottled water and toasted deli-type sandwiches may be small compared with those of its traditional

offerings of burgers and fries, but the world's biggest fast-food chain thinks its new products are contributing to growth as well as improving its image. Next year McDonald's will become the first fast-food chain to print nutritional information on its packaging.

Other companies have been less successful. Last month Wendy's, the third-biggest chain of burger restaurants, removed fresh-fruit pieces from its menus. These were introduced with much fanfare in February, but failed to meet sales targets. Some analysts think the withdrawal is because of the chain's problems in reviving its struggling business rather than the result of a flaw in the idea.

Both the advertising industry and America's Grocery Manufacturers Association want to preserve the present system of self-regulation. But advertising nowadays relies less on traditional media, such as television and magazines, and more on product placement, games on websites and, especially, “trade promotions”. These range from paying to have sweets placed where children see them to cut-price deals such as “buy-one get-one free”.

A survey last month by Britain's National Consumer Council found twice as many supermarket price-promotions are for fatty and sugary foods (usually branded, processed products that carry higher margins), than for fruit and vegetables. Because such promotions make junk food seem like more of a bargain, some health experts claim that they encourage poorer people to eat less well. But that does not have to be so. The council found that the top performer in cutting salt, nutrition labelling and removing sweets from checkouts, was the Co-op, a traditional British grocer with a larger than average share of budget-conscious shoppers (and a larger than average social conscience).

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS

Coke v Pepsi

Things go worse with Coke

Dec 14th 2005
From The Economist print edition

PepsiCo overtakes Coca-Cola in value

IN MORE than a century of hand-to-hand combat in shops, supermarket aisles, restaurants and bars around the world, Coca-Cola has nearly always been in the lead and Pepsi in second place. When Warren Buffett, Coke's long-time investor, told the board that he had visited a pizza parlour in Omaha, Nebraska, with his grandson only to discover it served nothing but Pepsi, Coke's bosses acted swiftly to remove their arch-rival from the menu and replace it with Coke.

If only the Atlanta-based company had moved as determinedly in response to changing consumer tastes, it might have avoided a humiliating reversal in fortunes. On December 12th PepsiCo overtook Coca-Cola in market capitalisation for the first time. With PepsiCo's share price having risen by 14% this year, its stockmarket value reached $98.4 billion, compared with $97.9 billion for Coca-Cola, which has seen its shares decline by 1.2% in the same period.

Pepsi is powered not by its traditional fizzy drinks—sales of those are flat—but such products as Gatorade, a sports-drink that has seen sales grow by more than 30%. Gatorade also represents a broader diversification by PepsiCo away from a reliance on sugary colas and into other products. PepsiCo now reportedly gets around 20% of its revenue from soft drinks, unlike Coca-Cola, where they account for some 80%.

Many of the brands that PepsiCo has been acquiring and promoting appeal to consumers' concerns about their health. PepsiCo's latest advertising programme promotes a new “Smart Spot” symbol, which allows people to identify healthier products. The spots are being attached to Gatorade and other PepsiCo brands such as Tropicana orange juice, Aquafina water, baked Lay's crisps and Quaker Granola Bars.

Coca-Cola will now try to regain the crown. Having endured various troubles and two chief executives since the death in 1997 of Roberto Goizueta, a much-admired boss, Coke brought a veteran, Neville Isdell, out of retirement last year to reinvigorate the company. Mr Isdell knows a thing or two about being in second place. In the 1980s he took Coke from the number two spot in the Philippines to move ahead of Pepsi.

Mr Isdell has Coke's own sports drink, Powerade, in his portfolio—but he could have had Gatorade. Five years ago another fizzy drink (champagne) was on ice, to celebrate Coca-Cola's $15.8 billion takeover of Quaker Oats, then owner of Gatorade. This takeover was supposed to lead Coke into what looked to be a hot new market for health drinks. But the “Sage of Omaha”, as Mr Buffett is known, blocked the deal, in part because it would have diluted the value of Coke's shares. PepsiCo took over Quaker Oats instead—a memory that must leave Mr Buffett and other Coke shareholders with a bitter taste in their mouths.

Economist.com BUSINESS

Corporate tax

Sighs of relief

Dec 14th 2005
From The Economist print edition

A long-awaited court ruling has big implications for European companies

A FEW years ago Marks & Spencer (M&S), a venerable British retailer, caused outrage in Brussels when it shut its local store, as part of a programme of shop closures across continental Europe. A condolences book was opened in the Brussels branch in the run-up to the closure—British customers filled it with anxious queries about where they were going to get their knickers in future; Belgians filled it with angry denunciations of the evils of Anglo-Saxon capitalism.

Now M&S is suddenly popular again in Brussels—but this time at the headquarters of the European Commission, rather than in the city's shopping arcades. That is because a long-running court case that M&S took out against the British government has, in the commission's view, protected the European Union's single market—and opened tantalising possibilities for increasing the commission's power over corporate taxation.

The M&S case flowed directly from the closure of its European stores in 2001. The company's bosses wanted to claim relief against taxes payable in Britain for the losses they had incurred elsewhere in Europe. The British government resisted, fearing that conceding this principle might lead to huge falls in tax revenue, as British companies juggled their books to make sure that losses elsewhere in the EU minimised their tax liability at home. M&S decided to take the case to the European Court of Justice in Luxembourg. Its verdict was awaited anxiously not just by the British, but also by other European governments such as Germany and the Netherlands, which were also worried that they might lose billions in revenues as new opportunities opened up for tax arbitrage.

In the event, the European Court's ruling—delivered on December 13th—was appropriately judicious. M&S, it said, could indeed claim tax relief in Britain on losses incurred elsewhere in the EU. But—much to the relief of the British government—the court was careful how it defined the circumstances in which such relief could be claimed. It ruled that a company could claim tax relief at home only after it had exhausted all the possibilities of claiming relief in the countries where its subsidiaries trade. This would appear greatly to limit the ability of companies to pick and choose where they pay their taxes. M&S was able to claim losses incurred in Belgium and France back in Britain, because it had ceased trading on that side of the Channel. Where a subsidiary is still a going concern, the host country's tax authorities have to be the first port of call.

The British government said the ECJ ruling was limited enough to make it unnecessary for there to be a wholesale rewriting of the British tax code. But the reaction to the ruling in official circles in Brussels will put the British on their guard. Both the commission and the majority in the European Parliament regard the ruling as strengthening the case for greater “clarity” on corporate taxation in Europe. In particular, they are pushing for a common corporate tax base across the EU. The British (and Irish) have long suspected that any such measure would be but a prelude to across-the-board harmonisation of corporate tax rates—upwards. Even Marks & Spencer would not welcome that.

Economist.com BUSINESS

American multinationals

Stars and stripes for ever

Dec 14th 2005
From The Economist print edition

American firms seem to have ridden a rise in hostility to the United States

EVER since the outbreak of the Iraq war, American companies have been braced for a consumer backlash in the rest of the world. Opinion surveys showed a surge in anti-American feelings in Europe and the Middle East after the outbreak of war in 2003. Anecdotal evidence also suggested that American companies were feeling the consequences of increased hostility to the United States. But one of the first detailed empirical studies, by Peter Katzenstein of Cornell University and Robert Keohane of Princeton University, debunks the idea of a backlash against American companies. Brand America may be suffering in the eyes of the world, but American brands are still prospering.

They're lovin' it

Sales in Europe, $bn *(% of total sales)*

Company	2000-01 average	2002	2003	2004
Coca-Cola*	3.9 *(23)*	5.3 *(27)*	6.6 *(31)*	7.2 *(33)*
McDonald's	4.8 *(33)*	5.1 *(33)*	5.9 *(34)*	6.7 *(35)*
Nike†	2.5 *(27)*	2.7 *(28)*	3.2 *(30)*	3.8 *(31)*
Adidas-Salomon	2.7 *(50)*	3.0 *(49)*	3.8 *(54)*	4.3 *(54)*
Cadbury Schweppes	2.8 *(41)*	3.4 *(43)*	4.6 *(44)*	5.3 *(43)*
Nestlé	15.7 *(32)*	18.0 *(31)*	21.2 *(32)*	23.0 *(33)*

*European sales include Eurasia and Middle East
†European sales include Middle East and Africa
Sources: "Anti-Americanisms in World Politics", Peter Katzenstein, Robert Keohane and Scott Nicholas Siegel; *The Economist*

That sales of firms closely identified with the United States have not fallen overseas is, in some ways, surprising. Messrs Katzenstein and Keohane cite a December 2004 poll, conducted by Global Market Insite, in which thousands of consumers in eight countries (Canada, China, France, Germany, Japan, Russia, Britain and the United States) were asked two questions about 53 American companies: would they avoid American products because of recent American foreign policy and military action? And to what extent did they see particular companies as "extremely American"? Overall, 20% of European and Canadian consumers said they were consciously setting out to avoid American products.

The firms most vulnerable to consumer boycotts included American Airlines, United Airlines, General Motors, Wal-Mart, CNN, American Express, McDonald's, Coca-Cola, PepsiCo and Marlboro. Nike was not far behind. Immediately after the invasion of Iraq, several press reports trumpeted boycotts of American goods in Europe. Will Hutton, a British economic journalist, asserted that the centre of the boycott movement was in Germany and that "the boycotts and the surrounding avalanche of negative publicity are a storm warning of what may lie ahead." News organisations from Reuters to the *Financial Times* reported that American firms such as Coca-Cola and McDonald's were seeing their sales fall in Germany and elsewhere in Europe.

Professors Katzenstein and Keohane have taken a more systematic look at the data. They studied the revenues of three big American-based consumer-products companies—and three of their European competitors—in Europe and the Middle East between 2000 and 2004. The American firms were Coca-Cola, McDonald's and Nike. The three European firms—Adidas-Salomon, Cadbury Schweppes and Nestlé—were chosen because they compete in the same industries. As Messrs Katzenstein and Keohane note: "If anti-Americanism had a significant impact on sales, one should find US-based firms' sales falling in 2003-04, when anti-American views rose sharply in Europe, compared to 2000-01...This fall in the sales of American firms should occur both in absolute terms

and relative to the performance of European firms."

In fact, the opposite happened (see table). Between 2000-01 and 2003-04 all six firms increased their European sales. American companies also grew at least as fast as their European rivals. Why should this be? It could be that American firms have adopted clever marketing strategies that counteract any surge in anti-Americanism. Or perhaps it is simply that European consumers are still capable of drawing a clear distinction between President Bush and a Big Mac.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS

The film industry

End of the dream

Dec 14th 2005 | LOS ANGELES
From The Economist print edition

Why Spielberg is paramount

Reuters

Katzenberg, Spielberg and Geffen: sweet dreams are made of this

“THERE are only three real brands in the movie business—Spielberg, Pixar and Miramax—and Spielberg is number one,” says an executive at Viacom. Talk is cheap. But Viacom has just spent real money to welcome Steven Spielberg, the most commercially successful director in the history of cinema, to the Viacom family. Paramount Pictures, which is a Viacom subsidiary, will pay $1.6 billion to acquire DreamWorks SKG, an independent film studio founded 11 years ago by Mr Spielberg and two friends, David Geffen, a music mogul, and Jeffrey Katzenberg, a former executive at Walt Disney. The deal gives a timely boost to Paramount's morale and leaves rival executives at NBC Universal with red faces: after nine months of negotiations, they had assumed DreamWorks would be theirs.

“I can't stress how transforming an event this is,” enthused Paramount's chairman, Brad Grey, as he confirmed the deal. Maybe so: since he took on Paramount's top job in March, Mr Grey's biggest challenge has been to find new “content”. With Mr Grey now signing Messrs Spielberg and Geffen to three-year contracts, Paramount could soon enjoy the benefit of four to six “live-action” (as opposed to animated) movies a year from DreamWorks to add to Paramount's normal roster of 14-16 films. In addition, it will have the exclusive right to distribute films from DreamWorks Animation, spun off in a public offering last year, and to use the films' characters in TV shows for the next seven years. There is one surprise. Paramount, claiming that private-equity investors are already interested, intends to sell the DreamWorks live-action library—some 59 films—for between $850m and $1 billion.

The deal contains two messages. One is that however good its movies, an independent studio will struggle to survive. As Mr Geffen explained: “We had hoped to be able to make enough films to be able to rationalise the cost of being our own distributor. Sadly, we were never able to make enough films to make that economically sound.” Hence the willingness of DreamWorks to accept a suitor.

The second is that although Hollywood may now be controlled by corporate America, it does not always play by the suits' rules. Since Mr Spielberg has a long history with Universal and since David Geffen counts Ron Meyer, Universal's president, as one of his best friends, the deal was Universal's to lose. That it was indeed lost was because General Electric (GE)—NBC Universal's parent company—took a hard look at DreamWorks' record, decided that the potential return on investment was below the GE norm, and, according to DreamWorks, abruptly lowered the agreed $1.5 billion bid by around $100m.

Enter Viacom. While Mr Meyer frantically pressed GE to show some flexibility and seal an agreement, Sumner Redstone, the octogenarian chairman of Viacom, made friendly telephone calls to Mr Spielberg and his partners. Then, on December 8th, Mr Grey and Viacom's co-president, Tom Freston, flew with a Paramount contract by private jet from New York to Mr Spielberg's house in Los Angeles—and the deal was done. Proof once more that in the movie business schmoozing still counts.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Videoconferencing

The Halo effect

Dec 14th 2005
From The Economist print edition

Jeffrey Katzenberg's latest venture: videoconferencing that actually works

JUST as the firm he set up with two other Hollywood moguls was being sold to Paramount, Jeffrey Katzenberg announced a new venture: a high-end videoconferencing system developed by DreamWorks Animation in partnership with Hewlett-Packard. In an effort to cut down on travel and boost productivity, Mr Katzenberg looked into videoconferencing in 2001 and found it clunky, unreliable and fiddly. So he asked his boffins to devise their own system. They teamed up with HP and the result, launched this week, is called Halo.

Each Halo room costs $550,000 to create, and includes four high-definition plasma screens. The lighting, camera angles, wall-colour, acoustics and furniture are all designed to make two Halo systems feel like a single room when linked together, and to do away with the 15 minutes of messing around usually required to set up videoconferencing gear. HP manages the service, which costs $18,000 a room each month, and runs the high-speed network that ensures natural, delay-free conversations. “It's designed to create ‘as though you were there' collaboration,” says Mr Katzenberg. Instead of travelling to his office in Britain every three weeks, he now goes every four months. Halo is, in short, the videoconferencing equivalent of flying in the corporate jet.

DreamWorks now has nine Halo rooms, HP has 13, Advanced Micro Devices has two and PepsiCo has five. Procter & Gamble and Novartis have also signed up. HP hopes to sell more than 100 Halo systems next year. Users say that while previous videoconferencing equipment was rarely used, their Halo rooms are in use around the clock. Hector Ruiz, boss of AMD, says Halo has cut travel between his firm's facilities in California and Texas. Steve Reinemund, boss of PepsiCo, says that every chief executive to whom he has shown the system has decided to buy it, too. Indeed, chief executives are proving an unexpectedly potent marketing tool. How appropriate that videoconferencing should be sold by word of mouth.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS

Face value

Firefox swings to the rescue

Dec 14th 2005
From The Economist print edition

Mozilla

Mitchell Baker, trapeze artist and leader of an open-source web browser, is on a mission to keep the internet free

YOU may recall that about a decade ago a company called Netscape launched the internet era with a new killer application called a web browser; that Netscape was subsequently expunged by Microsoft, the world's largest software company; and that Microsoft's copycat browser, called Internet Explorer, has held, in effect, a monopoly ever since. Until recently, this “history” of the web was broadly correct. Yet something very odd is going on that may yet require history to be rewritten. And that has a lot to do with Mitchell Baker, formerly of Netscape but nowadays the “chief lizard wrangler” (sic) of a non-profit foundation called Mozilla, whose main product is a web browser called Firefox.

Firefox seemingly came out of nowhere in November 2004, and has since captured a market share of 8-10% worldwide—but close to 30% in Poland, Germany and a few other countries—almost entirely through word-of-mouth marketing. The rest of the market still belongs mostly to Microsoft. Still, Firefox's advances have already had their intended effect: to present web surfers with a viable alternative to the monopoly, and thus to restart much-need innovation in browser technology, even by Microsoft itself. “The browser matters; it's the piece [of the internet] that touches human beings,” says Ms Baker, whose asymmetrically cut swoosh of red hair is reminiscent (“by coincidence”) of the Firefox logo. “This area shouldn't be stagnant; it should be exciting,” she says. Thanks to Firefox, it now is.

Firefox's tale is a curious one. The closer one looks, the more it appears to be a cooler, hipper, and safer incarnation of the allegedly deceased Netscape. As a company, the old Netscape disappeared in 1998, when—eviscerated by Microsoft—it sold itself to AOL, where it still snoozes as an under-utilised brand. But Netscape's employees and the browser's source code did not

simply disappear. Rather, the people fanned out in a diaspora to other companies in Silicon Valley, and many of them continued to fiddle with their beloved browser. They made its code “open source”—code that is freely available to anybody who wants to make improvements and share these with everybody else. Thus the browser secretly lived on within an informal volunteer “project” called Mozilla, and eventually got the name Firefox.

Ms Baker gradually found herself the leader of this project. Perhaps this is because she is a somewhat unusual member of the Netscape diaspora. For a start, she is a woman in a community populated, as one (male) colleague puts it, by geeky males with “spare time and no social life”. Ms Baker herself has never even written code. She studied Chinese at Berkeley, and then became a lawyer—her role at the old Netscape was in software licensing. On all technical matters, she defers to Brendan Eich, her chief geek. “By personality, I don't second-guess” people, she says. Indeed, she hones this skill two evenings a week when she flies trapeze for fun (a discipline where second-guessing the catcher is not advisable).

And yet, she is the leader. What, actually, does that mean in an open-source community? “There's nothing that I could stick on a résumé that people would understand,” she says. “Create structures out of chaos,” is one way to put it. “Translate geek-speak into English,” is another, she says. “Wrangle the lizards” is her favourite description, whence her title. By this she means co-ordinating the 800 or so Mozilla volunteers (or “lizards”, since Mozilla's logo is a dinosaur), of whom many are on the payrolls of companies such as Google, Sun Microsystems and Red Hat, while many others are simply hobbyists.

The other big part of her job is to wear her tough-lawyer hat and provide the strategic and legal direction that Firefox needs to thrive alongside a company like Microsoft. Her biggest decision of this sort was to formalise the project in 2003, by turning Mozilla into a non-profit foundation, financed by donations and a share of search-related advertising. To this foundation, she this year added a corporate (but still non-profit) subsidiary, which now employs a small permanent staff of about 40 people. Ms Baker wants to make sure that competitors cannot use legal red herrings about trademarks, patents and the like to derail Mozilla's mission.

Upgrading the net

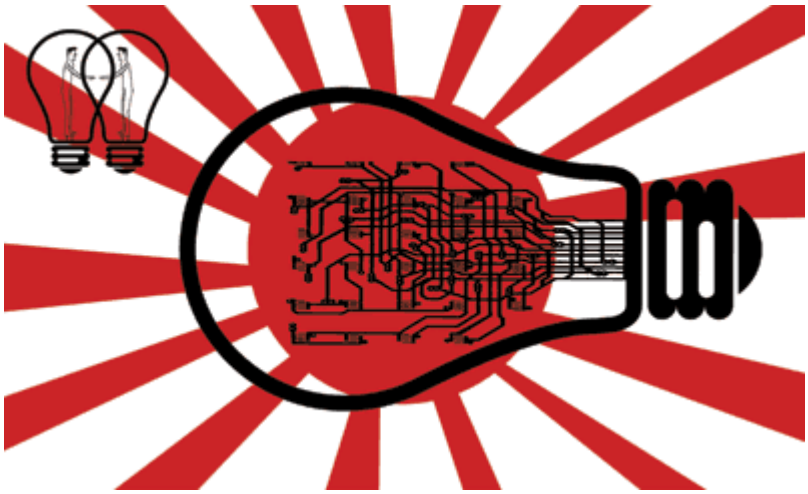
That mission, she emphasises, is obviously not to make profits or even, less obviously, to beat Microsoft. Instead, it is to make the web a better place by preventing anybody from turning it into a “monoculture”. In technology, as in ecology, monocultures are unstable. At the height of Microsoft's monoculture, its browser stagnated and became a security disaster waiting to happen, as hackers wrote nasty software to take advantage of web surfers. Firefox was safer from the start, and has become safer still with each new upgrade—the latest, version 1.5, was released on November 29th. Most users, after a few minutes of clicking around, also find Firefox more intuitive and practical—features such as tabbed browsing, where multiple web pages are stacked in the same browser window, tend to become compelling.

Ms Baker considers it a success that Firefox has already spurred Microsoft to invest again in browser innovation. This is crucial if the internet is to evolve to its next phase, she argues. Often dubbed “Web 2.0”, this will enhance users' experiences of the internet. For instance, technologies such as AJAX (short for “asynchronous JavaScript and XML”) supply applications that run on the internet with the same look and feel as applications that sit on the computer. And user-generated media such as blogs, podcasts and wikis are on the verge of mainstream adoption, promising an age of creativity. “Web 2.0 could have happened a lot earlier, if Microsoft had not had a monopoly for a decade,” says Ms Baker. Firefox, simply by existing, has done its bit to fix that.

The future of Japanese business

Competing through innovation

Dec 14th 2005 | TOKYO
From The Economist print edition



Japan's style of innovation failed it in software and biotechnology in the 1990s. It might work better in robotics, aerospace and other burgeoning technologies

IF JAPAN really is back, as its vaulting stockmarket suggests, then in which global businesses will its companies excel? Growing numbers of investors and onlookers have been asking this since the summer, as evidence has mounted that an economic recovery really is under way (see article). It is both a refreshing question and an important one. Refreshing because, for most of the past 15 years, the chief inquiry about Japan has been when it would finally exit from its debt-driven deflationary funk; important because, now that Japan is finally returning to health, investors and foreign rivals want to know whether its firms will regain some of their once fearsome competitiveness.

The tempting answer is that those foreign rivals can breathe easy. The end of deflation in Japan, which now seems imminent, will be much better for the country's domestic economy than for its exporters and multinational companies. Inflation will lead to higher sales at home, and lift the price of domestic assets such as property and shares; but it will not give a dramatic boost to firms competing overseas.

To thrive away from home, Japanese companies will instead have to innovate. On the face of it, they look capable of meeting that challenge. After all, they have pioneered and perfected many of the most advanced manufacturing and industrial technologies. Some of their futuristic visions were on display this summer, at the world expo that Japan hosted in Aichi prefecture. More than 22m visitors went to Aichi to imagine a world in which robots are part of everyday life and technology is the Earth's best friend. Along with the robots that Japan hopes will one day give directions, collect rubbish and babysit, are prototypes of robots that will be used in health care and search-and-rescue.

While visitors queued up to get a glimpse of Aichi's robots, they were surrounded by technologies designed to help the environment. As you might expect in an exposition dedicated to “nature's wisdom”, the latest solar cells powered parts of the site; the shuttle buses were equipped with fuel cells; and a power plant converted waste into energy. To beat the summer heat, the Aichi site also featured a range of new building materials and techniques that aim to keep down the temperature without energy-wasting air conditioners. These included walkways made of recycled materials; ultra-fine sprays of dry mist; and roofs coated with titanium-oxide, which lets water evaporate rapidly to lower the ambient temperature.

And yet, in spite of Aichi's extravagant display of new ideas, Japan and its companies no longer have a reputation as world-beating innovators. This, say the country's detractors, reflects an “outdated” way of doing things—a lack of creativity, flexibility and risk-taking. As a result, Japanese firms are no longer able to stay at the forefront of the most important and profitable new industries.

Japanese firms have not counted for much in software, the internet, biotechnology and other high-growth industries over the past decade. Japan can boast no equivalent of Microsoft, Google, Amazon or eBay. Its entire software industry has failed to make an impression on the world. Its best-known internet company, Softbank, is better at shuffling paper investments in subsidiaries than at inventing new technologies or business models. The new kid on the block, Takafumi Horie, head of livedoor, is most famous for three failures: a failed takeover bid for a baseball team, another for a broadcasting company, and an unsuccessful campaign for a seat in parliament. Although a handful of Japanese pharmaceutical firms have developed a few profitable drugs, Japanese companies are also far behind the rest in biotechnology and medical devices.

Japan's lack of success is not for want of trying. The country continues to lead the world in research and development, investing 3.2% of its GDP in R&D, compared with 2.6% in America and 2% in the European Union. Moreover, unlike western countries, where government and university labs generate lots of breakthroughs, Japan performs more of its R&D in big companies. An official at the once-mighty ministry of economy, trade and industry complains that METI's entire R&D budget is no bigger than that of Toyota. That is one reason why so many Japanese firms are near the top of the global tables for technology patents (see chart 1).

Turning Japanese 1

Top US patent award recipients, 2004

	Number of patents	2003 rank
IBM	3,248	1
Matsushita Electric	1,934	4
Canon	1,805	2
Hewlett-Packard	1,775	5
Micron Technology	1,760	6
Samsung Electronics	1,604	9
Intel	1,601	7
Hitachi	1,514	3
Toshiba	1,310	13
Sony	1,305	10

Source: US Patent and Trademark Office

Instead, the country's failure has much to do with its method of management and organisation. This won extravagant praise in the 1980s, when western writers and businessmen flocked to Japan for answers, and when the “lean” production manufacturing techniques pioneered by the likes of Toyota changed the world. The Japanese way of running companies has since fallen out of fashion, however. And although Japanese managers are slowly getting a little younger and nimbler, partly in imitation of American norms, the leisurely pace of business reform seems no match for the rapid rate of change in cutting-edge industries. Japan also suffers from a stifling environment for technology start-ups and a rigidly bureaucratic university research system that is poorly connected to the private sector.

New ventures needed

These are daunting disadvantages—as plenty of Japanese businessmen, scientists and politicians

acknowledge. Indeed, Japanese officials and business leaders have taken the first steps towards remedying some of them. A few Japanese bankers have set up funds to promote venture capital (or at least what passes for it in Japan). The government has also converted all of Japan's national universities into public corporations, in a bid to shake up scientists' civil-service mentality and make them more flexible and innovative. New clusters and consortia are popping up all over the Japanese islands, to promote better links between university laboratories, government budgets and corporate R&D. Between 2000 and 2003 the number of start-ups created to commercialise discoveries at Japanese universities rose from 315 to 800.

Although these efforts may eventually bear fruit, it will clearly take a while. Yet to focus on the slow pace of reform in Japan is to miss an important point: that there are many ways to innovate, and no single approach is “right” for all times and technologies. Japanese companies are already very good at—indeed, lead the world in—many types of innovation. The reason they lost their edge in the 1990s is not so much because their approach to innovation was “wrong”, as because it was ill-suited to the sectors dominating that decade. The next few years could easily be different, since the battle over next-generation technologies may well be in areas that suit the Japanese far better than biotech and software ever did.

In biotech and software America gained a clear edge from its ability to let lots of start-ups experiment with new techniques and business models, and to commercialise ideas from university research laboratories as quickly as possible. America's other advantage is in basic scientific research. Its universities dominate rankings of the best in the world and are well integrated with government and business laboratories. In other technology-heavy sectors, however, including several that Japanese companies are betting on, the university laboratory and the entrepreneur's garage have less of an advantage over a big Japanese corporation with extensive business experience and a giant R&D budget.

The American start-up method works very well when hundreds or thousands of potential business models might succeed—and the best way to find out which is to allow each brave or disgruntled genius to try out his own approach. Many fail, but a few succeed.

In other industries and technologies—such as cars and electronics in the 1970s and 1980s—a better way to innovate is to learn by doing. If 100 start-ups try, all might fail before they learn anything useful or before they come up with a product or service they can sell. A big company is often better suited to such fields. Not only can it offer its innovators a more reliable source of investment capital, but it also has links to consumers, which it can use quickly to improve the next generation of whatever it is making. A big company in a new field can afford to make products with initial drawbacks, provided it learns quickly to overcome them.

As they once did in cars and electronics, Japanese companies are today pursuing future technologies in several industries by making things first and only then pausing to think about how to improve them or put them to new uses. This leaves them at a familiar disadvantage in blue-sky research. But the idea—which has worked well enough in other industries to turn Japan into the world's second-biggest economy—is to keep getting better, eliminating costs and boosting quality, while rivals in America and Europe waste precious time at the drawing board. When Japanese companies do it right, they can innovate so quickly that they leave western competitors gasping for air.

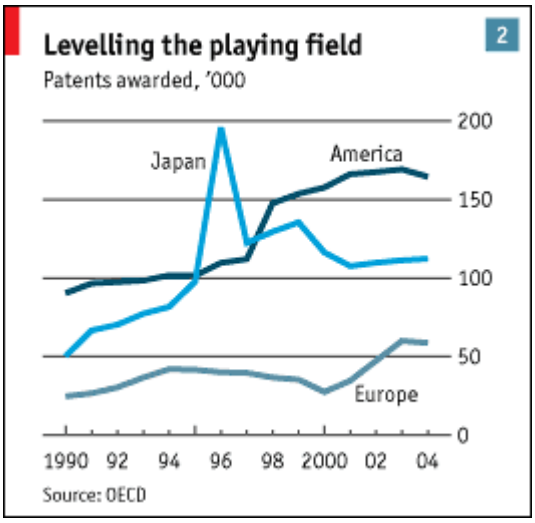
Sunny side up

One example that has received little attention is solar cells. Critics of the technology argue that it is not cost-effective and therefore cannot make any headway against other power sources without huge government subsidies in a few countries (notably, Japan and Germany). The doubters

conclude from this that solar energy is a pipe dream, hardly worth the effort. Japan's manufacturers turn this thinking on its head. Instead of waiting until the price is low enough to promise a market, they are relentlessly attacking the technology now, in an effort to drive down costs more quickly through trial, error and continuous innovation.

This is happening faster than most people realise. Prices of solar panels for residential use have been falling by 7% a year over the past decade, according to Cambridge Energy Research Associates (CERA), thanks largely to manufacturing improvements in Japan. CERA attributes most of the cost cuts to economies of scale and incremental improvements in efficiency, as Japanese manufacturers have designed ever-thinner components while continuously lowering their defect rates. This is exactly the sort of method that enabled Japan to gain an edge in other industries, from semiconductors to LCDs, and to hang on impressively against fierce competition from lower-wage countries.

This is no coincidence. The four biggest Japanese solar companies—Kyocera, Sharp, Sanyo and Mitsubishi Electric—are electronics firms and know from experience that these techniques work. These four firms now earn roughly $1 billion in combined revenues from their solar businesses and they are continuing to expand their capacity. CERA reckons that prices will keep falling rapidly, and that by the end of the decade solar energy may be able to compete with other forms of residential power—even without subsidies.



As with solar technology, many of Japan's biggest companies are investing heavily in a few high-tech fields that they hope will turn into huge new markets. Along with its continuing interest in cars and IT-related gadgets, corporate Japan is especially keen on three market segments: aerospace, robotics and technologies that either go easy on the environment or help to clean it up. The first of these markets, aerospace, is already big globally, but has mostly been dominated by American and European firms. The other two are small, but Japanese firms expect demand to grow sharply during the next few decades. Japanese researchers—like their rivals in America and Europe—are also investing heavily in nanotechnology, hoping that a mastery of all things tiny will help them make better integrated circuits and materials, which they can then use to transform a wide range of industries.

Man or machine?

Japan's biggest, and some of its most familiar, companies are leading this technology push. Some of the most eye-catching humanoid robots, for example, are being developed by car companies such as Honda, electronics firms such as Sony, and big technology groups such as Mitsubishi Heavy Industries. The same collection of carmakers, electronics companies and industrial firms are leading the charge into new environmental technologies, including fuel cells, solar cells, energy-saving building materials and methods for cleaning up water pollution. And as Japan advances into aerospace, its big electronics companies (such as NEC and Toshiba, which have formed a joint-venture, NT Space) and its industrial firms (Mitsubishi Heavy Industries, Fuji Heavy Industries and others) are at the forefront.

In aerospace, the Japanese have less experience than their American and European rivals, whose governments are also further ahead in blue-sky research. But they are trying. In October the Japan Aerospace Exploration Agency (JAXA) successfully tested a supersonic jet over the desert in

South Australia. Japan's last attempt to make the thing fly, in 2002, ended in an explosion. Similar failures have plagued Japan's rocket programme, stalling the country's plans to launch commercial satellites. But none of this has deterred JAXA or Japan's industrial firms, which have aerospace ambitions ranging from commercial aviation to space exploration.

Along with Japan's mastery of electronics and integrated technologies, those companies are counting on advanced new materials to give them an edge in aerospace. Consider Toray Industries, Japan's biggest textile company. Many of its products—such as airbags for cars and colour filters for LCDs—are high-value items. So despite falling demand for its futon fillings, Toray's operating profits rose by more than 40% last year.

Since margins in today's best segments will eventually shrink, however, Toray is investing heavily in new ultra-light and flexible composite materials to replace, among other things, the aluminium tubes used in commercial aircraft. Instead of worrying about Chinese competition in T-shirts and trousers, as western textile firms do, Toray is helping to make Boeing's new 787 commercial jets.

Altogether, Japanese firms will provide 35% of the Boeing 787, making entire wing sections from ultra-light composites before they are shipped to Seattle for assembly. The main contributors, besides Toray, are Mitsubishi Heavy Industries, Fuji Heavy and Kawasaki Heavy. In Japanese fashion, they are hoping that huge investments and lots of practice will give them an edge.

They are not just practising with Boeing. More than 20 Japanese firms will be involved in building the A380, Airbus's new jumbo jet. With the experience it is gaining and the investments it is making, Mitsubishi Heavy Industries (which made the “Zero” fighters Japan flew in the second world war) plans eventually to start building its own mid-sized commercial jets. That segment is dominated by Canada's Bombardier and Brazil's Embraer. Mitsubishi is also among those co-operating with America on missile defence; and it is leading Japan's (so far unsuccessful) drive to put commercial satellites in space.

Japan's high-tech companies are pursuing a similar approach to other technologies. Toyota, which views battery-and-petrol-driven hybrid vehicles as a stepping stone to even more fuel-efficient cars, has already begun testing fuel-cell vehicles in America. It will keep working to perfect the technology, even as American rivals such as GM and Ford struggle to compete with Toyota's hybrid models.

Japanese manufacturers such as Honda, Sony and Mitsubishi Heavy Industries are hoping that robots will succumb to the same approach to innovation that they have used on cars, electronics and industrial equipment. Although other rich countries are also doing research in robotics, Japan is far ahead in developing robots with humanoid features. Japanese companies are betting that, as these get smarter at walking, talking, dancing and being useful they will become the coolest and priciest toys in many homes. When it walks up to you, studies your face and greets you, Sony's humanoid prototype, QRIO, bears little resemblance to the firm's other consumer-electronics gadgets. The only hint of its true lineage is its one-hour battery life. But QRIO is an integrated device and Sony will keep tinkering with it and improving it in the same way that it once did with the CD player and the Walkman.

Look to America

In all of these areas, Japan's advantages should help its companies to avoid the problems that beset them in the 1990s. Nevertheless, the country can still learn from America, where researchers pay close attention to the market and are rewarded for success, and in which small firms are always popping up with bright new ideas. Some Japanese technology managers are trying to learn from this, as well they should. With an ageing population that will begin shrinking

by 2007, Japan has also failed to tap a ready source of potential new researchers. Just over 10% of Japanese researchers are women, compared with one-third in America and more than a quarter in Britain, France and Italy.

There is no guarantee that consumers will demand the sorts of products that Japanese companies plan to make. Robots are an obvious gamble. While Japanese researchers struggle to make them ever more life-like, some clever American company (Dell Robots, perhaps?) may find a cheap way to sell simple and functional robotic devices that consumers are more likely to want—outside Japan, at least.

For all the challenges they face, however, the future for Japan's big companies is not as grim as the 1990s made it seem. China has mastered the T-shirt and America dominates the internet. Japan has the technology to put up a good fight over much of what lies between.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com FINANCE & ECONOMICS

Private equity in Germany

Anglo-Saxon attitudes

Dec 14th 2005 | FRANKFURT
From The Economist print edition

Germany's fast-growing private-equity industry is dominated by big foreign investors. Home-grown firms cannot compete—and don't much want to

IN EUROPE last year an unprecedented €37 billion ($46 billion) poured into new private-equity investment. More than half of this was in Britain (see chart). Elsewhere a native private-equity culture is permeating only slowly. In Germany, Europe's biggest economy, less than €2 billion was raised by local private-equity funds in 2004, although another €5 billion was added in the first half of this year alone, according to BVK, the country's private-equity association.

Even this splash of capital, however, is no match for the big, foreign (mainly American, some British) private-equity firms that dominate Germany's market for corporate buy-outs. This year's top deal, the purchase by Britain's Terra Firma of Viterra, a property portfolio, from E.ON, a utility, was for €7 billion. Foreigners continue to be attracted by the low valuations of German companies and by the lack of competition from industrial buyers.

Divisions that big groups want to sell, or firms that have overreached their own funding capacity, tend to end up these days in the hands of one of a dozen or so well-known private-equity firms. What is more, after a bout of cost-cutting and restructuring, they are often sold on to another private-equity outfit.

Just look at this month's wheeling and dealing. Kohlberg Kravis Roberts (KKR) and EQT, a Swedish private-equity house, have been bidding against MAN, an industrial buyer, for MTU Friedrichshafen, an engine-making division of DaimlerChrysler. KKR bought MTU's aero-engine cousin from DaimlerChrysler in 2004 and listed it on the Frankfurt stock exchange this year. Kabel Deutschland, a cable-network operator, is being sold by two private-equity firms, Goldman Sachs

Capital Partners and Apax, to another, Providence Equity Partners. And Lone Star, a specialist in non-performing loans, ended up as the successful bidder for AHBR, a mortgage bank threatened with liquidation.

Many Germans wonder whether all this dealmaking is good for them. MTU's workers have been demonstrating against the prospect of KKR's proprietorship. Earlier this year a prominent politician fumed that foreign “locusts” were stripping companies bare.

In fact, the swarm of private-equity firms is doing the economy some good. Granted, their plans sometimes go awry and their quarry is left with a heavy burden of debt or they are forced into a hurried resale. But any self-respecting private-equity buyer aims to cut costs, rationalise business processes and increase a company's value—all of which is overdue at many German companies. A dose of rigorous cost analysis and a shake-up of fossilised management have quickened the country's corporate culture. The “locust” remark and the political debate that ensued prodded private-equity firms, by nature a publicity-shy lot, to explain themselves more clearly. More Germans now seem to recognise that private equity is to be encouraged rather than vilified.

Which may explain why Germany's new government, sworn in last month, favours the nurturing of an indigenous private-equity industry to compete with the Anglo-Saxons. That won't be easy. German venture-capital and buy-out firms, of which there are about 20, have tended to concentrate on the small end—companies worth less than €200m. Only one, Allianz Capital Partners, an arm of Germany's biggest insurer, has joined in big deals, worth €600m or more, of which Germany sees about ten a year. The country's first private-equity funds were run by banks, which focus on income from lending rather than on equity gains, and their successors are only gradually learning to serve investors' appetite for high capital returns. When it comes to seeking returns, “there is nothing more brutal than an American pensioner”, comments a seasoned dealmaker.

Like the foreigners, German private-equity firms aim to cut companies' capital expenditure and increase their cashflow. However, several factors reduce the pressure on short-term performance. One is Germany's tax regime: company owners are liable for “trade tax”, levied by municipalities; losses carried forward are treated unfavourably; and there is value-added tax, of 16%, on management fees. Although quite a few German citizens are active in big-league private equity, they tend to reside abroad in order to avoid VAT as well as income tax. As a result, German private-equity firms have concentrated more on medium-term growth.

“We don't restructure and we don't do start-ups,” says Jens Odewald, who runs Odewald & Compagnie, a private-equity firm in Berlin. His staff are predominantly former business managers rather than financiers. Mr Odewald himself was chief executive of Kaufhof, a German retail chain. “We look for growth companies with good managers,” he says.

Equita, a private-equity firm started by the Quandt family, which owns 47% of BMW, also emphasises the long term. It has started an “evergreen” fund that intends to buy companies and keep them if they do well, rather than sell after four or five years. However, it may discover, as do most other private-equity firms, that because the incentives for managers are based on realised returns, the temptation to sell sooner rather than later is strong.

Changing gear

Even so, German private-equity managers are starting to aim for the sort of returns that Anglo-Saxons have come to expect: 20-25% after tax. The prices of companies are creeping up, sometimes to seven times earnings before interest, tax, depreciation and amortisation (ebitda); leverage also sometimes hits seven times ebitda. Insurers, among others, are showing an appetite as other alternatives, such as hedge funds, begin to disappoint. There have even been issues of securities linked to private equity and aimed at retail investors.

However, it is not clear how far a private-equity mentality will pass beyond the buying and selling of big companies, or bits of them, and into the *Mittelstand*. Around 30,000 medium-sized firms have been marked as possible targets. Many of these are owned by their founders or the founder's family. Such people do not like to see their workers fired or their names disappear. Return-hungry financiers often lack the patience and tact required.

According to recent estimates, financial investors control or influence around 5,500 German companies. If all those investors were ambitiously managed private-equity funds, they would want to hold each company on average for perhaps five years. Thus, by simple arithmetic, 1,100 of these companies would be sold annually. The actual figure is far lower: only around 200 *Mittelstand* companies are sold by private-equity investors each year.

Demand and supply may yet change. The most exciting prospect for some is the estimated €250 billion-300 billion of pension liabilities on corporate Germany's books that have yet to be diverted into pension funds. If only a sliver of this finds its way into alternative assets, says Tom Pütter, head of Allianz Capital Partners, “imagine the impetus it would give the private-equity market”.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com FINANCE & ECONOMICS

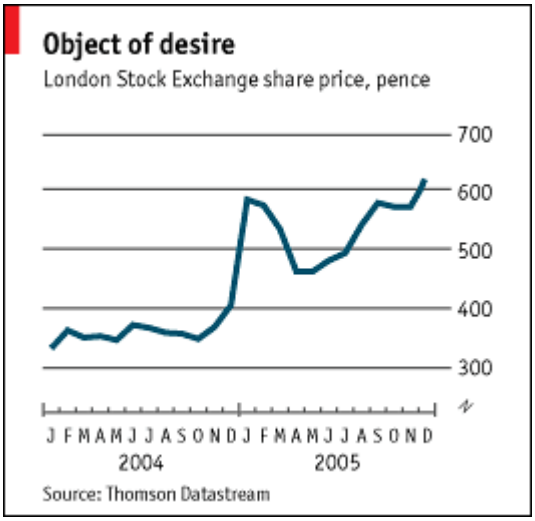
Stock exchanges

All roads lead to London

Dec 14th 2005
From The Economist print edition

Takeover speculation heats up again at the London Stock Exchange

Get article background



CONTRARY to some perceptions, the City of London is no respecter of tradition. Threadneedle Investments might sound like a firm that has been kicking around the City's medieval streets for the past few centuries, but it was in fact founded a mere 11 years ago and is now owned by American Express. Last week it raised its stake in the London Stock Exchange (LSE) as part of another piece of iconoclasm—the intricate dance involving the exchange, its shareholders and a string of foreign suitors.

Threadneedle's reported purchase of nearly 300,000 LSE shares at 615p ($10.88) each, boosting the big fund manager's total stake by about 1% to more than 12%, not only secured its position as the exchange's largest shareholder but also pricked the fingers of Macquarie Bank, a prospective bidder. The day before, this Australian investment firm had voiced an interest in making a cash offer of only 580p a share for the LSE. Macquarie's figure, which was probably only an opening shot to test market reaction, got a hostile retort from the exchange itself, which called it “derisory”.

Early this week, now armed with financial data that the LSE shared with other suitors nine months ago, Macquarie was huddling with exchange users and considering whether to make a higher, official offer. Britain's takeover authorities had set a deadline of December 15th for the Australians to make a formal bid or go away. No such bid had been made as *The Economist* went to press on December 14th. But even if Macquarie chooses not to proceed, the LSE has other would-be purchasers.

In the past year the exchange has fended off informal advances from two continental exchange groups, Deutsche Börse and Euronext, although neither has abandoned its interest altogether. Both are sidelined for the moment, pondering the British competition authorities' requirement that they reduce their stakes in clearing and settlement operations before bidding. Some of their shareholders have suggested that, instead of chasing the LSE, Deutsche Börse and Euronext might do better to merge with each other.

Amid all this, the LSE has had a good year. A record 74.5m trades were made in the year to November, 23% more than in the previous 12 months. The exchange's share price closed at 615.5p on December 13th, up by 14% since Deutsche Börse tentatively offered 530p a share a year ago and well above Macquarie's suggested price. This has allowed the exchange to ridicule Macquarie's opener. “This is really quite bizarre, to say the least,” says one person at the exchange. “We've just come out of the worst bear market in a generation. This is not necessarily

the time for a cash-out." Euronext, for one, has hinted at an offer involving shares instead of cash, allowing a greater potential gain for the LSE's shareholders.

Concerns about Macquarie go beyond price. The Australian firm, which has grown rapidly, with investments in toll roads, airports and property, has no experience of running financial exchanges. Its unusual business model includes a series of listed trusts, which provide the parent company with a stream of fees. Some in Australia have questioned whether its rapid rate of growth can be sustained.

There has been speculation that any offer for the LSE, which Macquarie says it would probably pursue as part of a consortium, would involve a similar structure. Reports that a bid would be financed through debt have caused some to worry that a Macquarie-owned exchange would increase fees. Macquarie has tried to quell the fear that it would charge the LSE's users more than they pay now.

Whether or not Macquarie wins the LSE, the landscape will keep changing. America's NASDAQ, which bought Instinet, an American electronic market, last week and was in takeover talks with the LSE several years ago, says it retains a "keen interest" in Europe, where it competes with the LSE for listings. The era of national markets may be passing.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com FINANCE & ECONOMICS

A Japanese trading debacle

Please may I take it back?

Dec 14th 2005 | TOKYO
From The Economist print edition

Red faces all round

Reuters

Tsurushima considers the position

THE cost to Mizuho, Japan's biggest bank, of the “fat fingers” that mis-keyed a share trade at its securities arm looks like being less than the ¥40 billion ($330m) once feared. Several broking firms that took advantage of Mizuho's clumsiness were reported on December 13th to be considering repaying about two-fifths of that amount. That may be small consolation to either the bank or the Tokyo Stock Exchange (TSE).

At the start of trading on December 8th Mizuho Securities placed an order on the TSE to sell 610,000 shares of J-Com, a small recruiting agency it was bringing to market that day, for ¥1 each: it had meant to sell one share for ¥610,000, the initial offer price. The false order, indeed, was for 40 times more shares than J-Com had outstanding.

Having tried frantically to cancel the order and failed, Mizuho scrambled to buy the shares it had sold but did not own. Some of the nicest sharks in finance, including Morgan Stanley, UBS, Nomura Securities and Nikko Citigroup, detected blood in the water. Meanwhile, as rumours swirled, investors sold the shares of brokers who might have made the mistake (Mizuho did not own up until trading ended). They also sold more broadly, calculating that a troubled broker would unload its own holdings to cover its losses. The Nikkei 225-share average registered its third-biggest daily fall of the year (though it recovered to end December 13th at its highest since 2000).

Mizuho would undoubtedly have been in an even bigger pickle were it not for limits to daily share-price movements on the TSE. All the same, it is one of the very few Japanese brokers on the exchange sufficiently capitalised to withstand a large trading loss.

Indeed, Mizuho's reputation will be repaired sooner than that of the exchange, whose rules and systems are now coming in for intense scrutiny. Almost anywhere else in the world, says one international trader, such an aberrant order would have been spotted and could have been de-keyed. The debacle comes a month after a systems glitch closed the TSE for the best part of a day. It seems, after the exchange's dog days during the 1990s and early in this decade, that too little has been invested in upgrading systems that have since been strained by a doubling of trading volumes. It all makes a mockery of the TSE's ambitions to seek a listing itself.

The TSE's regulator, the Financial Services Agency, is incandescent, and has demanded that the exchange improve its systems. After the exchange belatedly took upon itself some of the blame it had earlier directed wholly at Mizuho, its president, Takuo Tsurushima, said he was thinking of resigning. On December 12th, the exchange's clearing house, the Japan Securities Clearing Corporation, said it would invoke provisions unused in half a century to allow Mizuho Securities to

settle in cash with buyers of J-Com shares. The price, ¥912,000 a share, must have been plucked largely from the air. It now seems that Mizuho will not have to foot the whole bill. It must be relieved to see a limit to its losses.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

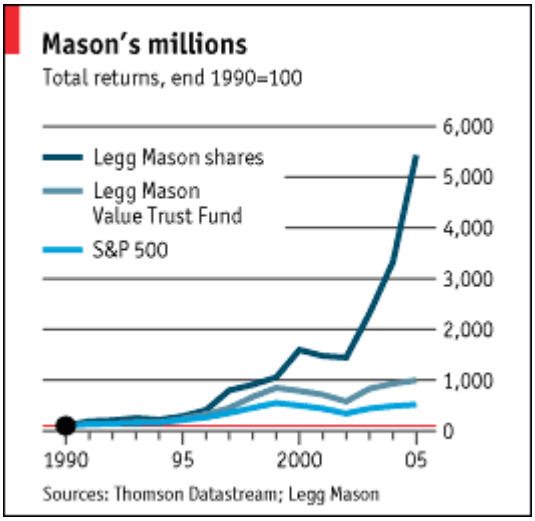
Economist.com FINANCE & ECONOMICS

Legg Mason

Its biggest bet yet

Dec 14th 2005 | NEW YORK
From The Economist print edition

The rise of an American broking firm



A DECADE ago, Legg Mason was the number-two brokerage firm in Baltimore. At the end of this year, it will be either the largest or second-largest listed asset manager in the world by many measures and perhaps the most successful. The transformation has had a bit to do with luck, a lot to do with one man's stockpicking record and most of all to do with another's company-building strategy. That strategy has now culminated in a huge bet on financial globalisation.

To Americans pondering a choice of mutual fund, Legg Mason has become well known because of the investing record of William Miller. For the past 14 years, his fund, the Legg Mason Value Trust, has beaten the broader market benchmarks, often by the kind of tiny margins that make horse races interesting and often because Mr Miller takes unusual positions that prompt others to rethink their own styles of investing.

Once again the Value Trust and the market are neck and neck in December, and once again Mr Miller's stewardship has been distinctive. Earlier in the year his fund trailed the market because of a low weighting in oil companies. Mr Miller reckons oil is overpriced at anything above $40 a barrel, partly because he thinks it is less scarce than most other investors do.

The fund has bounced back because of its heavy concentration on a handful of technology stocks, such as Google, Amazon and eBay, which Mr Miller sees less as growth companies (the conventional view) than as natural monopolies. He also has large positions in J.P. Morgan Chase and Citigroup, with growth prospects he thinks underrated at a time when the rise in interest rates is coming to an end and the American (and global) economy still looks strong. In short, Mr Miller tends to disbelieve headlines. Fortunately for his investors, he has on average been right.

Mr Miller, however, is not the best investor at the firm. That title belongs to his boss, Raymond “Chip” Mason. Like Mr Miller, Mr Mason's success has been based on making unusual and optimistic bets. Some of these have been small, such as hiring the inexperienced Mr Miller as an assistant manager on a new mutual fund in 1982. Some have been quite big, such as the acquisition, over 20 years, of a string of ever larger asset-management companies. The latest is enormous: this month's swap of Legg Mason's 1,500-strong traditional brokerage unit for Citigroup's investment-management arm, which oversees assets worth $400 billion. Mr Miller's success has brought Legg Mason fame and about $40 billion in assets; Mr Mason's deals had brought $400 billion in assets even before the deal with Citigroup.

The asset swap suited both sides. Legg Mason's retail distribution network was fairly small;

Citigroup's was vast. Legg Mason's asset-management results have been superb; Citigroup's have been mostly undistinguished, as often happens with brokers' in-house products. When a financial adviser can recommend a proprietary fund to a client, a clear conflict of interest arises. This had become explicit in the recent investigations sweeping through Wall Street. The scale of Citigroup's funds under management was hard to reconcile with their performance. The giant bank was anxious to get out of the regulatory glare and re-establish a reputation for objectivity. It initiated the deal.

Mr Mason, who has been concerned about such conflicts for years, saw his chance and took it, but his move amounts to more than opportunism. Already, he says, the managing of bonds has become global; equities, he believes, might go the same way within five years. As he moved Legg Mason away from broking into asset management, he began to count more big endowment and corporate-pension funds among his clients. These customers, he says, want investment firms that can operate in every financial centre. Legg Mason had already begun building outposts abroad, but it was hardly global in the manner of the mighty Citigroup.

Citigroup should be able to make its half of the deal work. It will have to integrate Legg Mason's brokers into its network: that is tricky, but Citigroup has done it before. Legg Mason has also integrated firms before, but $400 billion is a lot to swallow. The stockmarket is giving Mr Mason, thanks to his record, the benefit of the doubt. Perhaps the biggest worry is that he is now 69 and will not be around for ever. The better his record becomes, the more irreplaceable he seems.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com FINANCE & ECONOMICS

Microcredit and disasters

Starting over

Dec 14th 2005 | DELHI
From The Economist print edition

When you've lost everything, you need a grant rather than a loan

THE United Nations named 2005 the Year of Microcredit. In much of Asia, it was the Year of Disaster Relief. It began just after the devastating tsunami that killed hundreds of thousands and wrecked millions of livelihoods from Indonesia to Somalia. Then, after the annual monsoon floods, an enormous earthquake in Kashmir in October inflicted on Pakistan a catastrophe of even greater logistical difficulty. In both cases, huge sums poured into the relief effort. The fast-growing and fashionable industry of microcredit—the provision of tiny amounts of finance to people of little means—might seem an obvious vehicle for transmitting it to the poor. Only up to a point.

In fact, the very idea of using microcredit for relief work seems almost heretical to some purists, for whom the whole point of microfinance is that it is not charity, but a self-sustaining means of helping people start or expand a small business. If micro-lenders start dabbling in disaster relief, they send confusing signals about their real business.

Yet Syed Hashemi, of the Consultative Group to Assist the Poor, a microfinance consultancy, told a conference in Delhi last week that many donors and aid agencies assumed microcredit was “the answer” to the problems left by the tsunami in the places it shattered, such as Aceh, on the Indonesian island of Sumatra. He says that lenders, who may themselves be badly hit by a disaster, are best advised to limit their involvement in relief work. Similarly, governments and donors should avoid muddling aid and credit by offering cheap loans. If people have lost everything, they probably need to be given money, not lent it. “To disguise this through a subsidised loan undermines the whole operation.” After grants, a phase of cash-for-work (on reconstruction, say) is often needed before microcredit comes into play.

Not many microfinance institutions offer the services that people need most after a catastrophe: insurance, and access to their savings and to remittances from their families and friends. However, there is also a demand for income-generating assets—fishing-nets, tools, bicycles, stocks for a small shop, and so on—and hence for microcredit to finance them.

In the remote parts of Pakistan worst hit by the earthquake, where 300,000 people have been affected, there are fewer than 10,000 “active” microfinance loans. Yet in tsunami-hit Sri Lanka, where there was a large existing microcredit network, it has played a big if controversial role. The government and foreign donors have been lending at a concessional rate of just 3% a year to banks and microfinance institutions, which have been lending on at 6%.

Alessandro Pio, in Sri Lanka for the Asian Development Bank, which has helped finance this, concedes it is not a perfect solution. It is, though, a good way of reaching the fishermen, stall-holders and others who need small business loans. For a lender wanting to help, there is little choice but to match the existing subsidies. But it is hard for subsidised lenders to revert to lending on commercial terms; and because the banks and microfinance institutions are taking all the credit risk, most of the money flows to known customers.

Even what look like post-disaster success stories are ambiguous. Vijayalakshmi Das, of Friends of Women's World Banking, an outfit based in the Indian state of Gujarat, describes how, after a terrible earthquake there in 2001, it lent about 10m rupees ($210,000) to farmers. The loans, of about 100,000 rupees, 20 times the Friends' normal credits, financed water-pumps, seeds and tools and were all paid back within a year. But the group's mandate is to help women and poor households. Lending to farmers was a job that banks should have done.

Friends could help because it was quick and flexible, and active in the area. This should be the great strength of microfinance institutions. One lesson of the year of disaster relief is about the limits to what microfinance can achieve. But a more important one is the need for more of it.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Oil prices

Decisions and dilemmas

Dec 14th 2005
From The Economist print edition

Hoping and betting that oil continues to be expensive

Get article background

TODAY'S high oil prices are unambiguously good for neither producing countries nor the big oil companies. Both are rolling in money, of course, but the unpredictability of future prices makes investment decisions especially tricky. This week the world's oil cartel was pondering what it could do to keep prices up and a big oil company placed what amounted to a large bet on the cartel's success.

When ministers from the Organisation of Petroleum Exporting Countries (OPEC) met in Kuwait on December 12th to discuss new output quotas, they faced a dilemma: would pumping more oil mean more profit, or would it risk a price collapse? Oil prices had seemed set to rocket after hurricanes battered America's energy infrastructure, yet they have dropped by $10 a barrel or so from the peak, of around $70, they reached four months ago.

This fall may have persuaded ConocoPhillips, an American oil company, that this was a good moment to spend its cash pile. High prices tend to inflate the cost of oil assets, and so oil companies have been shy of acquisitions lately. But this week ConocoPhillips unveiled the $36 billion cash-and-shares purchase of Burlington Resources, a smaller American rival that produces natural gas and has benefited from high oil prices. Whether this triggers other such deals depends largely on how OPEC now manages oil prices.

The cartel's dilemma arises because, contrary to popular perception, the world never was especially short of crude oil this year. The bottleneck pushing prices higher was in American refining capacity and petrol stocks. The hurricanes in the Gulf of Mexico knocked out a lot of America's refineries, but the industry responded admirably. That is one reason prices have eased from the $70 peak.

Another reason for the fall is that OPEC, keen to avoid any appearance of post-hurricane profiteering, kept pumping as much as it could. And although prices fell a bit, they did not plunge as they had in 1998.

This week OPEC decided not to change its members' quotas. It will meet again at the end of January, when it may think about curbing output with a view to holding prices up. The cartel has reason to worry. First, according to a report by the International Energy Agency (IEA), crude stocks are growing fast. Second, oil demand has a seasonal tendency to cool in the second quarter. Third, a lot of new, non-OPEC production is due to come onstream soon. Finally, spare capacity, which was looking scarce, has grown. The IEA estimates that OPEC's spare capacity will rise from a record low of 600,000 barrels per day (b/d) at the end of 2004 to around 3.1m b/d by the end of next year.

OPEC seems keen to prop up prices above $50 a barrel. If it looks as if it will succeed, other

companies may be tempted to follow ConocoPhillips's example and pay handsomely for pricey oil assets.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Preparing for catastrophe

Bunker mentality

Dec 14th 2005
From The Economist print edition

Financial firms in Britain are armoured against disaster. Well, mostly

Get article background

BENEATH an innocuous green hillside in southern England, under 2.5 metres (eight feet) of steel-reinforced concrete, banks of hard drives buzz and hum. Operators, their eyes glued to computer screens, scan attentively for any sign of attack. Some miles away, tucked behind chain-link fences guarded by attack dogs and protected by airlocks, napalm-proof vents and steel blast doors, network servers collate and store encrypted data. You could be forgiven for thinking the cold war had never ended.

Welcome instead to the booming business of computer network security and disaster recovery. Across the country, companies such as Symantec, a producer of anti-virus software, and the Bunker, which safeguards critical data, are taking over nuclear shelters built by the Ministry of Defence.

It may all seem a little paranoid, but not to the regulators of London's financial industry. A study published this week by the Financial Services Authority, the Bank of England and the Treasury suggests that Britain's financial sector is well placed to cope with terrorist attacks, natural disasters and other big disruptions. The report complements a simulated attack carried out two weeks ago to test the responses of both emergency services and financial institutions. The idea this time was to examine what plans firms have to move their operations to back-up sites and to resume critical functions such as settling and clearing trades.

On the whole, the report's conclusions are reassuring. The bulk of Britain's core financial infrastructure can be recovered within two hours of a disaster. Within four hours it can be operating at between 60% and 80% of normal capacity. Give firms a day and almost all services, including trading and retail payments, can be back to normal.

But some of its findings are decidedly worrying. Although most firms have invested in redundant computer systems, only half have plans to cope with casualties among their staff and only half of these have tested such plans. Almost half of the critical sites identified in the study are located within ten kilometres (six miles) of the Bank of England. These include both primary computer sites and their back-ups and almost three-quarters of them are within five kilometres of the Bank. That makes them all vulnerable to a single catastrophic event.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com FINANCE & ECONOMICS

Economics focus

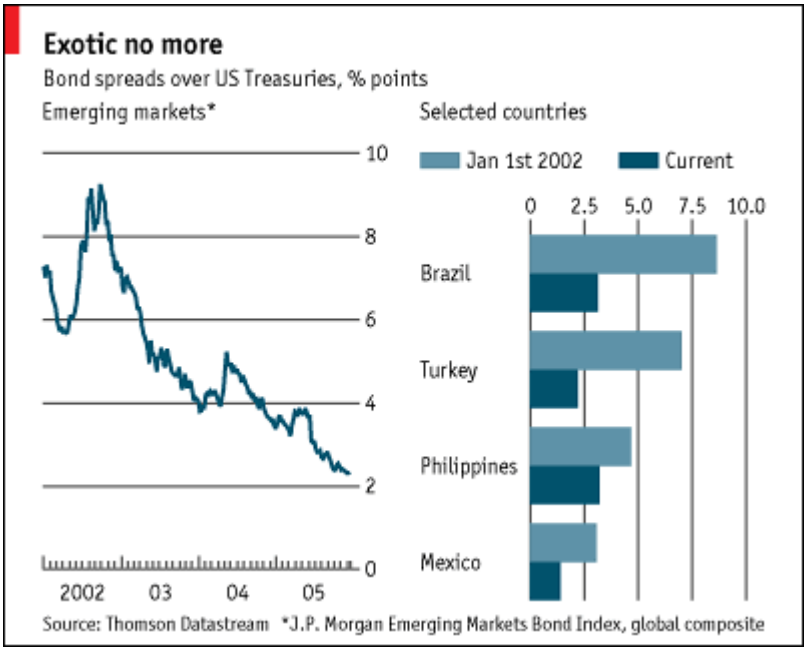
Middle-age spread

Dec 14th 2005
From The Economist print edition

More mature relations with foreign creditors are benefiting emerging markets

EMERGING markets are alternately courted by foreign capital and savagely rejected by it. Many of the luminaries who assembled on December 9th-11th at Templeton College, Oxford for the first annual meeting of the Emerging Markets Forum bear the scars of this torrid relationship. The forum—chaired by Fidel Ramos, former president of the Philippines, and Michel Camdessus, once managing director of the IMF—brings together veterans from ministries, markets and multilaterals, in a room where no one is trying to sell a bond or secure a bail-out.

Not that emerging markets are struggling to do either these days. Mexico's government has already raised the foreign money it needs for 2006 and 2007. It can now borrow almost as cheaply as its northern neighbour. The spread on its debt—the premium it must offer investors above the yield paid on American Treasuries—is little more than a percentage point. Last month, spreads on J.P. Morgan's index of emerging-market bonds (the EMBI Global) fell below 2.3 percentage points, the lowest on record (see chart). According to economists at Goldman Sachs, countries such as Brazil are borrowing at margins not seen since Britain was the world's banker and gold its standard of value.



Why are spreads so narrow? The commonplace answer is “global liquidity”. With interest rates so low for so long, yields in the rich world have grown flat, stale and unprofitable. Investors have

sought higher rewards on chancier investments farther afield. Their custom has pushed up the price on emerging-market debt and narrowed the spread. In 2001 two IMF economists calculated that a 1% fall in American ten-year yields subtracted 0.78% from the spread demanded by buyers of emerging-market bonds in the secondary market.

But Treasury yields are no longer falling. The ten-year rate is now back near its 2002 average, and yet spreads on emerging-market debt are still 4.9 percentage points below theirs. In a recent study, Mike Buchanan and Mónica Fuentes, two economists at Goldman Sachs, calculated that "virtually none" of the narrowing of spreads since the end of 2002 can be explained by the search for yield.

What, then, can explain it? Faster growth, lower inflation and tighter public finances in most emerging markets (outside central Europe) have played a role. Also important is a greater appetite for risk among investors. But 27% of the compression in spreads, reckon Mr Buchanan and Ms Fuentes, is due to a change in the "investor base", a shift in who the buyers are, not just in their willingness to pay.

Out of my class

Emerging markets, it seems, are appealing to a different class of suitor these days. Traditionally the preserve of adventurous cosmopolitans and reckless opportunists, these markets have now claimed a place in some of the more staid and parochial portfolios. In the first half of the year institutional investors, such as pension funds, allocated $7.3 billion to strategic investments in emerging markets, according to the IMF, a 73% increase over the first half of 2004. Funds dedicated to emerging markets have enjoyed large inflows of money, even as their traditional rivals—junk-bond funds—have suffered heavy outflows.

At the Emerging Markets Forum, the private-sector participants pointed out that this broader class of investors has changed the nature of the courtship between buyers and issuers. Whereas in the past, foreign creditors sought only a short-term commitment; the new money seems prepared to stick around. Panama, Peru and Brazil have all succeeded in exchanging near-dated securities for longer-dated instruments this year. Poland had the audacity to issue a 50-year bond.

By tradition, foreigners have also demanded repayment in hard currency. But as this dollar- and euro-denominated debt has grown more expensive, international investors have been drawn to local alternatives. Overseas buyers hold more than a fifth of Turkey's lira bonds, according to the IMF, and almost a quarter of Poland's zloty securities. Uruguay, Colombia and Brazil have all issued international bonds in their own money. Last month, Mexico sold warrants that gave holders of its dollar bonds the option to switch into peso debt in a year's time. Currency risk, after all, has an upside as well as a downside.

Will these new suitors prove faithful? Goldman's Mr Buchanan and Ms Fuentes are optimistic. It takes time and money to get to grips with a new asset class, they note, and these costs are irrecoverable. Thus investors' new commitment to emerging-market debt should outlive the circumstances that first motivated it. As rich-world interest rates return to more normal levels, the search for yield becomes less pressing and foreign investors will prove more demanding. But the Goldman economists argue that "a moderate sell-off in emerging markets would not see all this new money rushing back to its old haunts."

The Emerging Markets Forum, however, concluded on a more wistful note. The relationship between emerging markets and global capital may be more stable than it was. But it is also less rewarding than it should be. However strong the flow of private capital from abroad, the forum noted, it continues to be more than matched by public flows in the opposite direction. Emerging

economies will add more than $400 billion to their foreign-exchange reserves this year, according to some estimates, and their net exports of capital will near $200 billion. Rich-world investors have shown themselves willing to buy emerging-market assets at high prices, in local currencies and at lengthy maturities. Yet the flow of capital out of poorer countries is greater than the flow in. The challenge for emerging markets, the forum-goers concluded, is not only to seduce and tame overseas capital, but also to put their own savings to better use at home.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com SCIENCE & TECHNOLOGY

Climate change

Pricking the global conscience

Dec 14th 2005
From The Economist print edition

A UN conference on global warming makes progress, sort of

Get article background

JEAN CHRÉTIEN, a former prime minister of Canada, described his country's relationship with its giant southern neighbour as like sleeping with an elephant. It was, he observed, good to have a few others around to watch the elephant as well. An important United Nations (UN) conference on climate change, which has just concluded in Montreal, showed just how right he was.

For two weeks, negotiators from nearly every country in the world converged on the frozen Canadian metropolis to discuss the future of the Kyoto protocol. That controversial UN pact obliges many industrialised countries (but notably not the United States) to cut their emissions of greenhouse gases (GHGs) by a fixed amount below their 1990 levels by 2012. The treaty's 150-odd signatories had hoped to map a rough outline of what should come after the treaty's first commitment period.

In the event, the American delegation strenuously opposed them, insisting that it was too early to contemplate life after Kyoto. Then, in shockingly undiplomatic language, Paul Martin, Canada's prime minister, denounced the American position and invoked the need for a “global conscience” to deal with this most global of problems. America's chief negotiator stormed off in a huff, throwing the meeting into chaos. The talks looked destined to fail. Then something odd happened that persuaded the elephant to dance.

Canada's friends came to the rescue at the last minute. Defying expectations, China, the biggest GHG emitter not to have an emissions target, and Australia, which also rejected the Kyoto treaty, agreed to talk about talks. Then Bill Clinton delivered a clever last-minute speech suggesting that

the Bush administration's position on climate change is out of touch with the sentiments of many Americans and with the actions of the many American states and corporations that are already cutting GHG emissions.

Finding itself isolated, the American delegation reluctantly returned to the negotiating table—and, after an all-night session, a compromise deal was announced on December 10th.

Life after Kyoto

The final pact is not quite the “historic agreement” some green groups claim, but it does, nonetheless, make progress in three broad areas. First, the signatories to Kyoto agreed on fiddly details essential for the implementation of the pact. For example, they accepted compliance rules that set out what happens if countries do not meet their targets. They also agreed on ways to improve the treaty's overly bureaucratic mechanism for rich countries to gain credits for reducing GHGs in developing ones and in former Soviet states.

Second, they agreed that future climate talks should take twin tracks. First, Kyoto signatories will now start negotiations on what binding emissions targets the rich countries of “Kyotoland” must accept for the second commitment period. These negotiations must be completed in time to ensure that there is no gap between the first round and what follows.

Second, everyone—including America—agreed to start talks on a possible UN climate pact that would include America and China. This is not as big a breakthrough as it might seem, for the American delegation insisted that mandatory emissions targets must not be part of these discussions. Even so, it represents progress of a sort, and it creates a UN process through which a post-Bush America could take on meaningful emissions targets.

The final, and largely overlooked, outcome of the conference may yet prove its most important: delegates agreed to promote carbon capture and sequestration technologies, and to get serious about adaptation to climate change.

Carbon sequestration matters because the world cannot simultaneously meet its energy needs and climate goals without developing technologies for using the vast global reserves of coal in ways that do not contribute to global warming.

Adaptation matters because even if future rounds of Kyoto succeed in bringing America on board, many aspects of global warming are already inevitable. The sea level, for example, will continue to rise for decades to come, with awkward consequences for much of humanity, especially in the poorest parts of the world.

The Montreal summit therefore deserves credit for bringing America back into the UN's climate negotiations. However, its enduring legacy may be greater still if it results in serious efforts around the world to adapt to the inevitable consequences of climate change.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com SCIENCE & TECHNOLOGY

Predicting earthquakes

Granite batteries

Dec 14th 2005 | SAN FRANCISCO
From The Economist print edition

Earthquakes may cause electrical surges—which might help predict them

THE inhabitants of San Francisco would dearly like to know when the San Andreas fault that runs by their city is going to snap again. But even after almost 12,000 geophysicists met there last week for the autumn conclave of the American Geophysical Union (AGU), they were little the wiser. Most geophysicists agree that earthquakes cannot be predicted, although every large one brings tales of animals sensing trouble hours beforehand and of people seeing strange lights.

No one knows what might cause such phenomena. Indeed, so many different mechanisms have been proposed as being behind the apparent warnings of impending disaster, that seismologists tend to look upon any claim with suspicion. There is, however, one set of observations that may yet receive a scientific imprimatur. This is the suggestion—yet to be confirmed by an unambiguous statistical analysis—that space-borne instruments such as France's *Demeter* satellite have seen changes in the radio waves of the ionosphere that coincide with, and sometimes precede, earthquakes in the ground below.

In the light of this suggestion, Friedemann Freund, a physicist at San Jose State University in California, has stuck his neck out. As he told the AGU meeting, he thinks he knows what is going on, and it is this: if you squeeze a block of granite hard enough, it becomes a battery.

If he is right, an earthquake will generate enormous electrical currents in the ground—precisely the sort of thing that would upset the ionosphere and generate strange lights in the form of lightning-related phenomena. More to the point, it is possible that some of this power might be released before a fault moves catastrophically, and thus provide some warning of an earthquake.

The idea that squeezing crystals has electrical consequences is not new. A phenomenon called piezoelectricity, which is exploited in pressure sensors and quartz watches, involves creating a voltage between the ends of a piece of crystal by applying pressure. In this case, the voltage arises because the crystal deforms and a symmetry between positively and negatively charged atoms is disturbed.

Piezoelectricity, however, cannot sustain a sizeable current. So Dr Freund is proposing a different mechanism—similar to the one that goes on in the semiconductors from which computer chips are made. This mechanism relies on another phenomenon, called charge separation.

In many kinds of rock, most notably granite, the application of pressure and the resulting deformation of the rock's constituent crystals turn some of the oxygen atoms in those crystals into charge carriers. These atoms are missing an electron and are thus positively charged.

When the rock is further deformed, it becomes possible for these atoms, called “holes”, to steal an electron from a neighbouring atom, in effect shifting the hole. In this way, the holes can move through the rock. Indeed, they do this so easily, Dr Freund has calculated, that many of them move out of the section of rock under stress altogether, leaving it with a surplus of electrons.

Thus, a granite battery is charged.

The electrons from the stressed rock cannot follow the holes, because granite is not a very good conductor of this more usual form of electricity. But when, if you do this trick in a laboratory, you give the electrons the chance to bypass a section of rock by way of a metal wire, quite large currents will flow. Outside the laboratory, Dr Freund believes, the role of the wire is played by heated rock (at temperatures above 500°C, granite becomes conductive to electrons as well as holes).

Extrapolating from Dr Freund's laboratory experiments, the strain in a real-life geological fault such as the San Andreas could, as it shifted, generate hundreds of thousands of amperes per cubic kilometre in a fluctuating pattern that would cause very low frequency radio waves to be emitted, thus disrupting the ionosphere.

Whether such currents could act as earthquake predictors depends on whether there are changes in the strain on a fault before it slips. To date, no such changes have been detected, but Dr Freund argues that the strain gauges deployed at the moment are too near the surface to pick up shifts that happen at the depths where earthquakes occur. His electrical currents, by contrast, would be detectable by magnetometers at the surface as well as by satellites watching the ionosphere—if they do indeed exist in the ground as well as the lab.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com SCIENCE & TECHNOLOGY

Planet-hunting

ESP for ESPs

Dec 14th 2005 | BERKELEY, CALIFORNIA
From The Economist print edition

A way to detect Earth-sized planets around other stars

SINCE the days of Copernicus, astronomers have been telling humanity just how un-special it is. Demoted from the centre of the universe, the species orbits a normal, middle-aged star in a typical spiral galaxy of which there are perhaps 100 billion others spread throughout space. Over the past ten years, the heirs of Copernicus have even found that the sun is far from unique in playing host to orbiting planets. Although the “extra-solar” planets (ESPs) discovered so far are all larger than Earth, these astronomers think it is only a matter of time before Earth-sized ESPs are found. And that time may now be close at hand. For, if Grover Swartzlander of the University of Arizona and Dimitri Mawet of the University of Liège, in Belgium, are correct, the technology to see such planets has just been invented.

Until recently, astronomers have had to content themselves with indirect observations of ESPs. A planet has a gravitational effect on its host star. If the planet is heavy enough, the resulting wobble can be detected. Alternatively, a planet's orbit may cause it to pass between its star and the Earth. Again, if it is big enough, the resulting dip in the amount of starlight may be detectable. But on only three occasions has the light from an ESP been detected directly. Normally, the light from such planets gets lost in the glare of the parent star. It is this that the two researchers hope to change, using a complex lens called a vortex phase mask.

Dr Swartzlander first suggested the idea of such masks in 2001. He has now had one made, and is about to publish the details in *Optics Letters*. Mr Mawet, meanwhile, has come up with a different design for a mask, which he published last month in the *Astrophysical Journal*. Both designs, however, work the same way. They twist the light from the star so as to cause part of it to cancel itself out, leaving a dark window in the middle through which planets as small as Earth can shine.

Dr Swartzlander's prototype phase mask was made using the sort of etching techniques employed to fabricate computer chips. The result was to convert the surface of a glass plate into the shape of a spiral staircase with 16 steps. When light travels through glass, it slows down (the amount it slows is measured by a number called the refractive index). That means the parts of the beam falling on different steps are retarded by different amounts with respect to each other.

The mask is designed so that light passing through its thickest region is slowed by exactly two cycles compared with that passing through its thinnest. The result is that the beam twists as it passes through the spiral and interferes with itself. Peak falls on trough to create a core of darkness along the lens's central axis. However, because the light from any planet orbiting a star at which the lens is aimed directly is arriving from a point slightly to the side of that star, it is able to shine through essentially unaltered. Moreover, now that the glare of the star has been removed, that planet's glow is more easily discernible.

Mr Mawet's design is slightly different from Dr Swartzlander's. He plans to cut a series of concentric circles into the surface of a piece of diamond, a material with one of the highest refractive indices known. These circles, however, will serve to twist the starlight in much the same

way that the Swartzlander spiral does. And, while Mr Mawet's design is likely to be harder to fabricate than Dr Swartzlander's, because its features are smaller, it has the advantage that it should work with all wavelengths simultaneously, whereas Dr Swartzlander's will work with light of but a single wavelength.

Dr Swartzlander's prototypes have performed well in laboratory tests in which lasers played the parts of star and planet. In addition, he and his group have shown that their masks can be integrated into existing telescopes by fitting one to an instrument on Mount Lemmon outside Tucson, Arizona—though they have yet to put it to the ultimate test of collecting light from a known ESP, since the air in Arizona wobbles too much. Mr Mawet and his team, meanwhile, are trying to fabricate prototypes of their design to test on the European Southern Observatory's Very Large Telescope in Chile, which is at a higher altitude, and thus less prone to wobbling air.

Strictly speaking, vortex masks are not the only way to cancel the light from a star. It can also be done using an instrument called an interferometer. But a vortex mask requires only one telescope whereas an interferometer needs at least two, in order to combine, and thus cancel, several images. Both America's space agency, NASA and Europe's, ESA, have plans to launch missions to search for Earth-like planets during the course of the next decade. At the moment, NASA's *Terrestrial Planet Finder* and ESA's *Darwin* are designed around constellations of satellites configured as interferometers. The invention of vortex filters may, however, lead to at least a partial rethink. If it does, then when the Earth-like planets start to roll in, the astronomers responsible may be drinking their toasts with a twist.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com SCIENCE & TECHNOLOGY

Skiing

Not waxing lyrical

Dec 14th 2005
From The Economist print edition

Using ski wax can trap dirt, and thus slow down the skier

THIS season, like every previous one, recreational and racing skiers alike will apply wax to their skis in the hope of schussing that little bit faster. They will do so after assessing the air's temperature, its humidity and the prevailing snow conditions, so as to determine exactly which wax they should use. Not any old wax will do. Some are formulated for use over cold, dry snow and others for warmer, wetter stuff. Aficionados who want to extract the maximum advantage will take great care over which they choose.

But recent research suggests they are wasting their time, not merely in their choice of wax, but in bothering to wax their skis at all. A study by Leonid Kuzmin, a former cross-country racing champion turned ski coach who is now a doctoral student at Mid-Sweden University, concludes that for runs of more than a couple of hundred metres, the presence of ski wax slows the skier down. Admittedly, Mr Kuzmin's research was conducted on cross-country skiers, but he believes it will prove true for downhill racers as well.

The way in which a ski slides over the snow boils down to the way in which friction between the base of the ski and the surface of the snow melts that snow, transforming it into a thin layer of water. The ski then floats across this layer. Indeed, snowboarding, ice skating and sledging also rely on this principle.

The depth of the water layer is crucial. If it is too thin, which can happen at very low temperatures, the ski sticks. Skiers typically try to overcome this friction by applying hard wax. If it is too thick, which can happen at warmer temperatures, it can create suction that makes it harder to slide over the water layer. To avoid that, skiers typically apply soft wax.

The base layer of modern skis is made from a substance called ultra-high-molecular-weight polyethylene. This fantastic plastic has molecules far longer than those of regular polyethylene, and these molecules are, in addition, packed tightly into a crystal structure rather than being scattered at random. The result is a tough material that has a low coefficient of friction—comparable to that of Teflon—and is highly resistant to abrasion. Its properties are so useful and unusual that it is used not only to create the base layer of skis, but also to make bulletproof jackets and artificial hip and knee joints.

In fact, Mr Kuzmin suspected that this wonder material was so good that waxing it was no longer necessary. He therefore decided to conduct a series of experiments with waxed and unwaxed skis. He commissioned a few pairs of transparent skis that a volunteer then took out on to a test slope. That done, he examined the skis and found that those treated with wax attracted more dirt than the ones that were unwaxed.

Moreover, Mr Kuzmin also recorded the speeds the volunteer reached while gliding down the test slope. He found that after distances of just a couple of hundred metres, gliding on unwaxed skis was faster than on their waxed counterparts.

Skiers can thus, it seems, forget about long hours spent ironing wax on to their skis and devote more of their time to the slopes. Before ski-wax makers pack up shop, however, business opportunities do still exist. Mr Kuzmin's research pertains only to glide wax—that is, wax intended to make skis glide faster. Cross-country skiing also employs a second form, kick wax, which has the opposite effect.

Kick wax is applied to the parts of the blades of cross-country skis that are directly under the skier's feet. These do not (or, at least, should not) touch the ground when the skier is gliding. On flat terrain, such wax allows the skier to push off and on uphill climbs it prevents him from slipping backwards. Manufacturers will be pleased to hear that kick wax remains essential to cross-country skiing.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Online gaming

Worlds without end

Dec 14th 2005
From The Economist print edition

The online game industry is an excellent way to study the economics of fun

Synthetic Worlds: The Business and Culture of Online Games
By Edward Castronova

University of Chicago Press; 332 pages; $29

Buy it at
Amazon.com
Amazon.co.uk

Reuters

THE sci-fi dream of the computer-generated virtual reality—so familiar to readers of “Neuromancer” and viewers of “The Matrix”—has finally come true. But, as is often the case with guesses about future technologies, it has not come true in quite the way that many people expected.

While scientists developed sensory-input devices to mimic the sensations of a virtual world, the games industry eschewed this hardware-based approach in favour of creating alternative realities through emotionally engaging software. “It turns out that the way humans are made, the software-based approach seems to have much more success,” writes Edward Castronova in an illuminating guide to these new synthetic worlds.

Millions of people now spend several hours a week immersed in “massively multiplayer online role-playing games” (MMORPGs). These are often Tolkienesque fantasy worlds in which players battle monsters, go on quests, and build up their virtual power and wealth. Some synthetic worlds are deliberately escapist; others are designed to be as lifelike and realistic as possible. Many have a strong libertarian bent. Sociologists and anthropologists have written about MMORPGs before, but Mr Castronova looks at the phenomenon from a new perspective: economics.

Mr Castronova's thesis is that these synthetic worlds are increasingly inter-twined with the real world. In particular, real-world trade of in-game items—swords, gold, potions, or even whole characters—is flourishing in online marketplaces such as eBay. This means in-game items and currency have real value. In 2002, Mr Castronova famously calculated the GNP per capita of the fictional game-world of “EverQuest” as $2,000, comparable to that of Bulgaria, and far higher than that of India or China. Furthermore, by “working” in the game to generate virtual wealth and then selling the results for real money, it is possible to generate about $3.50 per hour. Companies in China pay thousands of people, known as “farmers”, to play MMORPGs all day, and then profit from selling the in-game goods they generate to other players for real money.

Land and other in-game property has been sold for huge sums: one “Project Entropia” player paid $26,500 for an island in the game's virtual world last year, and has already made his money back by selling hunting and mining rights to other players. Trade in virtual items is now worth more than $100m each year. In some Asian countries, where MMORPGs are particularly popular, in-game thefts and cheats have led to real-world arrests and legal action. In one case in South Korea, the police intervened when a hoard of in-game money was stolen and sold, netting the thieves $1.3m. In-game money is, in short, no less real than the dollars and pounds stored in conventional bank accounts.

Virtual economies are an integral part of synthetic worlds. The buying and selling of goods, as the game's inhabitants go about their daily business, lends realism and vibrancy to the virtual realm. But in-game economies tend to be unusual in several ways. They are run to maximise fun, not growth or overall wellbeing. And inflation is often rampant, due to the convention that killing monsters produces a cash reward and the supply of monsters is unlimited in many games. As a result, the value of in-game currency is constantly falling and prices are constantly rising.

Mr Castronova's analysis of the economics of fun is intriguing. Virtual-world economies are designed to make the resulting game interesting and enjoyable for their inhabitants. Many games follow a rags-to-riches storyline, for example. But how can all the players end up in the top 10%? Simple: the upwardly mobile human players need only be a subset of the world's population. An underclass of computer-controlled “bot” citizens, meanwhile, stays poor for ever. Mr Castronova explains all this with clarity, wit and a merciful lack of academic jargon.

Some of his conclusions may sound far-fetched. In particular, he suggests that as synthetic worlds continue to grow in popularity, substantial numbers of people will choose to spend large parts of their lives immersed in them. Some players could then fall victim to what Mr Castronova calls “toxic immersion”, in which their virtual lives take precedence, to the detriment of their real-world lives.

But perhaps this is not so implausible. It is already possible to make a living by working in a virtual world, as the “farmers” demonstrate. In one survey, 20% of MMORPG players said they

regarded the game world as their “real” place of residence; Earth is just where they eat and sleep. In July, a South Korean man died after a 50-hour MMORPG session. And the Chinese government has recently tried to limit the number of hours that can be spent playing MMORPGs each day.

As technology improves, players could make enough money to pay for the upkeep of their real-world bodies while they remain fully immersed in the virtual world. Mr Castronova is right when he concludes that “we should take a serious look at the game we have begun to play.”

Synthetic Worlds: The Business and Culture of Online Games.
By Edward Castronova.
University of Chicago Press; 332 pages; $29

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Popularising philosophy

Question marks

Dec 14th 2005
From The Economist print edition

AP

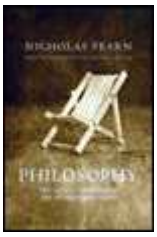
Orange or banana? Which am I?

THE urge to use “philosophical” as another word for “other-worldly” is unlikely ever to die out. But the gibe is heard less often today than it once was. Perhaps because there is less certainty around than there used to be or because there is more to be muddled about, philosophy's promise to clarify has growing appeal. Not that philosophers, God forbid, are making philosophy relevant. But people are recognising how much it touches their lives. A sign of the change is the growing appetite for books that popularise philosophy.

Close behind the news headlines lurk abstract puzzles. Freedom and democracy are offered up as justifications for war, yet they themselves are rarely explained or justified. People argue passionately about abortion, uncertain where law and morals meet or what anchors moral convictions. A judge in Dover, Pennsylvania, faced by Christian zealots claiming that evolution is “just a theory”, asks experts to explain what makes theories scientific.

Puzzles are all very well. But arguments have to end. When arguments themselves turn on contentious principles—majority rule, moral truth, science against faith—philosophy will not go away. Shut the door, and back it comes through the window. Philosophy, once readmitted, then turns a characteristic trick. It makes you think how you should be arguing about those principles and tries to make plain what should count as good and bad reasons. It guarantees no answers but does offer the wherewithal to recognise genuine answers when they

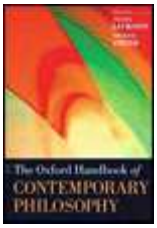
Philosophy: The Latest Answers to the Oldest Questions
By Nicholas Fearn



Atlantic Books; 304 pages; £17.99

Buy it at
Amazon.com
Amazon.co.uk

The Oxford Handbook of Contemporary Philosophy
Edited by Frank Jackson and Michael Smith



Oxford University Press; 720 pages; $99 and £55

Buy it at
Amazon.com
Amazon.co.uk

appear.

Thought of that way, philosophy becomes a scourge of non-answers whether from “our-faith-is-sacred” believers or from “I-respect-your-views” relativists. Coolly, it bats back corporate and political spin. It provides a shovel for the bullshit that abounds—a word Harry Frankfurt, a moral philosopher, recently chose as the title for a bestselling essay on the erosion of public discourse.

The subtitle of Nicholas Fearn's book is “The Latest Answers to the Oldest Questions”, a quiet tease. You may step into new philosophical water but the river is reliably the same. The focus is the human condition. His three sections are “Who am I?” (mind and body), “What do I know?” (language and knowledge), “What should I do?” (morals and the meaning of life).

As a populariser, Mr Fearn has many strengths. His style is brisk, not jaunty; he prefers sketching arguments to mapping intellectual camps or decoding jargon; he is up-to-date but not incomprehensibly cutting-edge. His preface on the history and purpose of philosophy is a small marvel. One novelty—he has written a similar book before—is material from philosophers he talked to. Offering philosophers in their own voice is an excellent idea. Bryan Magee set the standard here with “Men of Ideas” in 1978, from a television series. Unfortunately, Mr Fearn's mini-interviews, neither wholly dialogue nor wholly reportage, sit awkwardly in an otherwise commendable book.

You will search in vain for voices in “The Oxford Handbook of Contemporary Philosophy”. Pick a passage from any of its 29 entries; you will not know who is writing. Anatoly Karpov, a Soviet chess master, once boasted: “Style? I have no style.” Philosophers take equal pride nowadays in an absence of rhetorical effect. Arguments, circulated and refined like a chess opening 12 or 15 moves deep, are their stock in trade.

The handbook is the latest inspiration of Peter Momtchiloff, an editor at Oxford University Press who thinks philosophy should have a wider public. General reader, though, be warned. The book is demanding and difficult. Seven sections covering morals, politics, mind, language, metaphysics, knowledge and science make it as serious and thorough as a survey could be. A telling feature of entries on ethics and politics is responsiveness to empirical research. Philosophy to be any good has, in a sense, to be pure talk. But it also needs to keep an eye on the facts. To anyone prepared for the climb, the handbook promises a commanding view.

Philosophy: The Latest Answers to the Oldest Questions.
By Nicholas Fearn.
Atlantic Books; 304 pages; £17.99

The Oxford Handbook of Contemporary Philosophy.
Edited by Frank Jackson and Michael Smith.
Oxford University Press; 720 pages; $99 and £55

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BOOKS & ARTS

American 20th-century writing

Sharp-tongued woman

Dec 14th 2005
From The Economist print edition

LILLIAN HELLMAN, an American writer born in New Orleans 100 years ago, was never short of a comeback line. She wrote six or so Broadway plays, a dozen film scripts and four volumes of inventive, not to say fictionalised, memoirs. Her most famous words, though, were in a letter to the House Un-American Activities Committee (HUAC) at the height of the first cold war in 1952.

Lillian Hellman: A Life with Foxes and Scoundrels
By Deborah Martinson

Counterpoint Press; 448 pages; $27.95

Buy it at
Amazon.com
Amazon.co.uk

The committee had subpoenaed her as part of its campaign to expose the red menace in Hollywood. It wanted Hellman, a showbiz celebrity and erstwhile defender of the Soviet Union, to name communists she knew. She answered that she would testify about herself, not others: “To hurt innocent people whom I knew many years ago in order to save myself is, to me, inhuman and indecent and dishonourable. I cannot and will not cut my conscience to fit this year's fashions.” The bullies needed telling, and Hellman told them magnificently.

Critics right and left were quick to carp. Film people with more to lose than Hellman had defied the committee previously. She and her lawyer had deftly scripted her performance to keep her out of jail. Nobody else could remember a voice in the committee room crying out: “Thank God, somebody finally had the guts to do it,” as she later claimed. No matter. Hellman's HUAC appearance was her theatrical and moral high point. In a few crafted lines she had exposed the hearings for what they were: a ritual shaming.

What else Hellman should be remembered for is harder to pin down. As a teenager she developed a taste for high bohemia and a sense of being someone. Her father, a small businessman, was an easy-going gambler and philanderer, whom Hellman glamorised. Her mother belonged to a prosperous banking clan. Young Lillian studied drama in New York and drifted to Hollywood where MGM paid her a subsistence wage to read scripts.

At a party in 1930 she met Dashiell Hammett, the hard-drinking thriller writer and author of “The Maltese Falcon” and “The Thin Man”. They began an affair which lasted on and off until his death in 1961. Often at war, often apart—Gore Vidal once asked, “Did anyone ever see them together?”—and each with a string of other lovers, the pair were nevertheless close. Hammett urged her to write and virtually co-wrote her first plays. She nursed him through the lung cancer that killed him.

A communist, Hammett introduced Hellman to politics. They promoted the Soviet line until the late 1940s and paid a price for their cluelessness. Hollywood denied Hellman work. Hammett went to prison for five months in 1951 as an unco-operative witness, which broke him. By contrast the damage that Stalinist posturing like hers did the democratic left in America was something that Hellman never really acknowledged—a silence which makes her liberal epiphany before HUAC even more remarkable.

In the theatre Hellman's talent was for message plays with melodramatic plots. Her two hits came early: “The Children's Hour” in 1934, about a vicious schoolgirl who denounces her teachers for a gay liaison, and in 1939 “The Little Foxes”, an anti-capitalist parable about greed and corruption in an Alabama mill town. By the 1950s they were out of fashion. Hellman nevertheless enjoyed a long afterlife as a tigerish party-goer in literary New York. Her feel for the spotlight did not leave her. In her 70s, she modelled furs for Blackglama. When Mary McCarthy, a fellow writer, said on television that every word Hellman wrote was a lie, including “the” and “and”, Hellman sued for $2.5m, though she died in 1984 before the case came to court.

Deborah Martinson, Hellman's fifth biographer, recounts the facts of her life without finding a pattern. She shows no grasp of Hellman's times and writes atrociously. Through no fault of her own Ms Martinson never met Hellman. Had she experienced the stormy temper and gift for fable in person, she might have made more sense of this *grande horizontale* and chronic disturber of the peace who could seldom resist a cruel rejoinder or suppress a “How about it?” to somebody else's husband. Readers minded to pursue the Hellman legend would do better to read her memoirs, each of them brief, “An Unfinished Woman”, “Pentimento”, “Scoundrel Time” and “Maybe”—always remembering that they were not written on oath.

Lillian Hellman: A Life with Foxes and Scoundrels.
By Deborah Martinson.
Counterpoint Press; 448 pages; $27.95

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Terror in South-East Asia

Nailing a bombing

Dec 14th 2005
From The Economist print edition

In the Shadow of Swords: How Islamic Terrorists Declared War on Australia.
By Sally Neighbour
HarperCollins Australia; 432 pages; A$24.95

Reuters

The tears of Oz

ISLAMIC “terror” has spawned a cottage industry—nay, a castle industry—of experts. Bookshelves groan under the weight of their books; most can be ignored, and should be. “In the Shadow of Swords” is an exception.

After each of the recent major bombings—Bali, Madrid or London—the same questions remained. Who were these people so willing to kill innocent civilians? How did they overcome the logistical problems—procuring the bomb-making material, then assembling and delivering it? Sally Neighbour, an Australian journalist, addresses both of these issues in the context of the terrorist bombings of the two Bali nightclubs in October 2002, which killed 202.

That attack was the work of Jemaah Islamiah (JI), which was a movement long before it became an organisation. In the 1950s, its goal was to establish an Islamic state across South-East Asia. In the mid-1990s, when Osama bin Laden was seeking to expand his terror network, JI was a natural partner. Al-Qaeda had money, expertise and training camps, including some in nearby Philippines; JI, under the spiritual leadership of Abu Bakar Bashir, had the local connections.

Riduan Isamuddin, an Indonesian member of JI, better known as Hambali, was the link between the two organisations. At a meeting in Bangkok in February 2002, he told a small group that it had become too difficult to attack embassies. Henceforth, the group would concentrate on “soft targets”. The Bali bombing came ten months later. The chief bomb-maker was a man named

Azahari Husin, who was killed in a shoot-out with Indonesian police last month. Hambali was captured by the CIA in Bangkok in August 2003, and is now being held at one of the CIA's “black sites”.

Ms Neighbour's anatomy of the Bali bombing amounts to six days in the life of executing a terrorist attack. She has collected a mass of detail about how the nightclubs were picked—“lots of whiteys dancing there,” one bomber claimed afterwards—and also about what went wrong. Two of the men recruited to bring the bomb-laden vehicles to the site could not drive.

When Ms Neighbour went to a *pesantren*, an Islamist school in rural Indonesia where the minds of some of the Bali bombers were filled with radical, hate-filled, ideas, she noted: “The green-uniformed minions reminded me of Mao's Red Guards.” If there is a lesson in that, there is another in the fact that although America did its best to persuade the Indonesian government to arrest Bashir, the *pesantren* headmaster, Bashir's status locally had been enhanced by the pressure.

Ms Neighbour offers no grand prescriptions for dealing with terrorism, but her book is a compelling, readable and well-informed account of an Islamist terror network that has spread across South-East Asia.

In the Shadow of Swords: How Islamic Terrorists Declared War on Australia.
By Sally Neighbour
HarperCollins Australia; 432 pages; A$24.95

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BOOKS & ARTS

Conducting

Maestra Marin

Dec 14th 2005 | BALTIMORE
From The Economist print edition

The Baltimore Symphony did not like it when Marin Alsop was appointed music director, the first woman to run a major American orchestra. Can she win it over?

MOST nine-year-old girls want to play with dolls; Marin Alsop begged her parents for batons. Forty years later, as music director-designate of the Baltimore Symphony and the first woman to run a major American orchestra, it is her artistic vision that overshadows her oft-mentioned gender.

For orchestras with dwindling audiences and worrying budget deficits, the aloof, coat-tailed maestro rehashing his war-horses is no longer an attraction. Ms Alsop is a superb communicator and a conductor who appreciates the symphony orchestra as a flexible instrument, not just a symbol of past glories.

A protégée of Leonard Bernstein and a champion of new music, she has been pigeonholed for too long as both. Her work with the Bournemouth Symphony Orchestra, where she is principal conductor, as well as appearances with other orchestras on both sides of the Atlantic, have shown her to be a convincing and dynamic interpreter of repertoire staples as well. The first two CDs in her Brahms symphony cycle, with the London Philharmonic, are polished and invigorating.

On a train trip to Baltimore, the day of her 49th birthday and the morning after she had conducted Prokofiev and Brahms with the New York Philharmonic, Ms Alsop recalled being taken to one of their concerts as a child. She was just nine and became mesmerised by Bernstein. “It was like a religious calling. I never even questioned it, I just decided I wanted to be a conductor.” Her parents, both professional musicians, bought her her first batons. Her father still hand-makes all her batons, presenting her recently with 30 new ones.

Ms Alsop trained as a violinist at the Juilliard School of Music, but she always yearned to conduct. As a freelance violinist with the New York Philharmonic, she had watched conductors browbeat and embarrass individual players, and knew she could do better if given a chance. The road to achieving her dream was not direct, though. She was rejected for Juilliard's conducting programme, but soon founded her own orchestra, Concordia. In 1993 she was appointed music director of the Colorado Symphony, revitalising both the fledgling orchestra and its audience by often choosing new American composers, such as Michael Daugherty, Libby Larsen and Christopher Rouse, over older, better known European names.

The Baltimore appointment generated headlines; first, because she is a woman, and then when the orchestra players rebelled, complaining that they had not been adequately consulted in the search for their new music director.

It is never easy to please everyone and conductors have to satisfy many constituents: orchestra members, audiences, management, local critics, and, crucially in America, donors. Invariably, opinions clash. Lorin Maazel's appointment as music director of the New York Philharmonic in 2001, for example, elicited a collective whinge from local critics, but was enthusiastically welcomed by the orchestra. The challenge for Ms Alsop now is to turn the players into fans.

The “woman conductor” label propelled Ms Alsop into the spotlight. Although she is adamant about not attributing any of her professional struggles to her gender, she admits that being a woman has affected her approach to conducting. “You need clean lines and no filigree,” she says. An aggressive man is just that, but an aggressive woman can be pasted with nastier labels. Conversely, she says while turning her palms upward, some gestures make a male conductor look sensitive, and a woman look weak.

New York, New York

Ms Alsop has an ambitious, survivor mentality, though, and this has helped her face the humiliating thumbs-down from the Baltimore Symphony players, whom she had guest-conducted seven times. She describes herself as “forever a New Yorker, a fatalist optimist tinged with cynicism.”

A full schedule offers Ms Alsop good reasons to be confident. Since her appointment, she has already conducted in Boston, Sydney and Prague. She takes up her Baltimore post officially next month; the rest of 2006 will see her conducting in Cologne, London, Zurich and making her debut with the Royal Concertgebouw in Amsterdam, one of the world's greats.

Her confidence is visible also in her conducting style. Ms Alsop believes firmly that the music should be driven by the composer. “Brahms needs depth and richness and agility, while Beethoven needs transparency. When you think of Leopold Stokowski and the Philadelphia Orchestra, the string sound was the same in Mozart and Mahler and I don't strive for that.”

She warns that imitation is dangerous. “Conducting is a metaphor for who you are, and if it's affected and insincere, it becomes trite and inauthentic.” She has inherited Bernstein's habit of addressing the audience, and she often introduces new works with a few comments and a demonstration. A trim and elegant woman, on the podium she is enthusiastic yet precise, always turning fully to face the section she is conducting. Passionate without being flamboyant, her occasional small leaps don't initiate wild gesticulating. Off the podium she is equally professional, confident and articulate, with a wry humour.

As the train slows past the unkempt streets and boarded-up row-houses that greet the visitor to Baltimore, Ms Alsop's flashes her wry smile. “It's been a welcoming city on all fronts,” she says dryly. If any musician's determination, talent and charm can seduce a tough city, a reticent audience and affronted musicians, it will be Marin Alsop's.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com PEOPLE

Obituary

Eugene McCarthy

Dec 14th 2005
From The Economist print edition

Getty Images

Eugene Joseph McCarthy, a maverick presidential candidate, died on December 10th, aged 89

WHEN Eugene McCarthy was making his first and most famous attempt on the presidency, in 1968, he was often asked why he was running. It was a good question. And he had a good answer:

> Nor law, nor duty bade me fight,
> Nor public men, nor cheering crowds:
> A lonely impulse of delight
> Drove to this tumult in the clouds.

This fragment of Yeats seemed to epitomise the man who quoted it. Irishness, daring, puckish humour, wilful solitariness, a sense of the pervading importance of higher things, were all delivered with professorial elegance by a man once described as “Thomas Aquinas in a suit”. Two criticisms only could be made. First, that it was delivered in the white heat of one of America's nastiest election campaigns, to crowds chafing for more solid fare. And, second, that it was not true.

Mr McCarthy's peculiar political career was driven not by the impulse of delight but, in fairly equal measure, by principle and pique. His model of political behaviour was Thomas More, a witty but pig-headed martyr for his beliefs in Tudor England; his training ground was the hockey field at the various Catholic institutions at which he was educated, on which his desire to win could be shockingly intense. In political life, he kept his ambition well buried under layers of diffidence and urbanity. But he had some, and when he was slighted he did not forget.

His decision to oppose Lyndon Johnson in 1968 was a case in point. Mr McCarthy had come ardently to oppose the Vietnam war. He also could not help remembering that Johnson had humiliated him at the 1964 Democratic convention, choosing Hubert Humphrey, rather than him, as his running-mate at the last minute. He thought Johnson “a barbarian”, determined to barge his way through any kind of checks and balances to prosecute the war. But the Senate had no desire to curb him. Someone, therefore, had to take the debate to the public. That someone (no one else being brave enough) would have to be Eugene McCarthy.

His campaign was odd in the extreme. He did not call himself a candidate, but an “accidental instrument” to express the will of the country. He knew he could not win. By challenging Johnson, he simply hoped to force the convention open for someone else. In fact, he came so close to Johnson in the New Hampshire primary that the president realised he was doomed, and soon quit the race. The nomination went eventually to Humphrey, no improvement in Mr McCarthy's view. But he had managed to shake his party to its foundations.

He had also mobilised the young, inspiring them to shave off their beards and get knocking on doors in a way not seen again until Howard Dean's insurgency in 2004. The radicals of the anti-war movement did not take to him, however, nor he to them. As riots raged in the streets of Chicago at the 1968 Democratic convention, Mr McCarthy, watching from the windows of the Hilton hotel, said the scene below reminded him of the Battle of Lake Trasimeno in the Punic Wars.

Politics as football

He was a politician, yet he despised politics. In the House, where he sat for Minnesota's Fourth District from 1949 to 1959, he would pointedly read books in committee meetings. In the Senate, where he served from 1959 to 1971, he seemed bored, and was often absent. Instinctively shy, he hated pressing the flesh or canvassing for money. He once compared politics to being a football coach: “You have to be smart enough to know the game and dumb enough to think it's important.”

Was it important to him? His opinions could be hard to sift, sometimes far to the left of his party, sometimes conservative. He believed in “redistributive justice”, a relic of his youthful days in the Catholic Worker movement, but endorsed Ronald Reagan. He also opposed all limits on political donations as crimps on freedom of speech. That freedom was his passion in politics. Accordingly he hated the stale old bunfight between Republicans and Democrats, and left the Democrats in 1972 to become an independent.

His three later forays into presidential politics were embarrassing and looked self-indulgent. But Mr McCarthy believed he could still shake Americans out of their political torpor. The irony was that the Democrats, responding in part to the shock he had administered, became increasingly a party of the elite and intellectual rather than the working man.

He might never have entered politics at all. As a young man, he almost became a monk. In his home town, a small German-Catholic community lost in the Minnesota prairie, to take orders was the highest career. He tried the novitiate for a year, but was thrown out for intellectual pride.

The same pride tortured him in politics. His mind was too acute and freewheeling to suffer its restrictions. Norman Mailer, meeting him in 1968 at a fundraiser in Harvard, found him drooping and baggy-eyed, longing to be rescued. Some weeks later, he saw him in Chicago. He had just definitively abandoned the race, and was dining and joking with friends. He was free. And Mr Mailer suddenly glimpsed in him then the perfect president, “harder than the hardest alloys of steel”.

Overview

Dec 14th 2005
From The Economist print edition

The **Federal Reserve** raised interest rates by 0.25 percentage points to 4.25%. The statement accompanying the decision dropped some familiar watchwords and provided a new phrase or two to ponder. The Fed did not say, as it has on previous occasions, that monetary policy is accommodative, suggesting that rates may be nearing their neutral level. But it said that "some further measured policy firming is likely to be needed". After 13 rises in a row, the Fed's campaign is not yet over, but an end may be in sight.

Stockmarkets are finishing the year strongly. They reached their highest levels in 2005 in France, Germany, Italy, Japan and the Netherlands on December 13th, and in most of the other developed economies the week before. Morgan Stanley's index of stockmarkets around the world also reached a high for the year on December 13th.

The spirits of **America's consumers** have recovered from the summer's hurricanes. The Michigan index of consumer confidence rose to 88.7 in December, just shy of the 89.1 recorded before Hurricane Katrina. But households will still finish the year in lower spirits than they started it. Retail sales rose by 0.3% in November, in value terms, buoyed by sales of motor vehicles. An offsetting drop in spending at petrol stations was good news: a reflection of falling prices at the pump.

In the year to October industrial production fell by 2.7% in **Italy** and by 1.4% in **France**. In **Germany**, however, it surged by 3.8%. The news cheered investors. December's ZEW survey of sentiment among analysts and institutional investors jumped to its highest level since February 2004.

Japan's GDP grew at an annual pace of just 1.0% in the third quarter, according to revised figures, slower than initial estimates of 1.7%. But growth for the second quarter was revised up from 3.3% to 5.0%.

Japanese consumer confidence edged higher in November. Inflation, which remains absent from consumer prices, is evident in the production line. Prices for corporate goods rose by 1.9% in the year to November.

In **Britain** consumer-price inflation slowed to 2.1% in the year to November, from 2.3% in the year to October. The Bank of England left its key interest rate unchanged at 4.5%.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Output, demand and jobs

Dec 14th 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 2.6	Q3	+ 0.6	+ 2.6	+ 3.3	+ 0.7	Q2	+ 1.2	Q3	5.1	Nov	5.2
Austria	+ 1.8	Q3	+ 2.3	+ 1.6	+ 2.0	+ 1.6	Sep	+ 0.9	Sep	5.2	Nov	5.0
Belgium	+ 1.1	Q3	+ 1.7	+ 1.3	+ 1.8	– 7.7	Oct	+ 0.9	Sep	12.8	Nov†	12.8
Britain	+ 1.7	Q3	+ 1.6	+ 1.7	+ 2.1	– 1.8	Oct	+ 1.5	Oct	4.9	Oct††	4.7
Canada	+ 2.8	Q3	+ 3.6	+ 2.9	+ 3.0	+ 1.1	Sep	+ 2.2	Sep	6.4	Nov	7.2
Denmark	+ 4.8	Q3	+ 5.7	+ 2.4	+ 2.4	+ 4.6	Oct	+ 4.4	Oct	5.4	Oct	6.3
France	+ 1.8	Q3	+ 2.7	+ 1.6	+ 1.9	– 1.4	Oct	+ 0.5	Sep	9.7	Oct	10.0
Germany	+ 1.4	Q3	+ 2.5	+ 1.0	+ 1.5	+ 3.8	Oct	– 0.8	Oct	11.5	Nov§	10.7
Italy	+ 0.1	Q3	+ 1.1	+ 0.1	+ 1.2	– 2.7	Oct	+ 0.1	Sep	7.7	Jun	8.1
Japan	+ 2.9	Q3	+ 1.0	+ 2.4	+ 2.2	+ 3.0	Oct	+ 0.4	Sep	4.5	Oct	4.6
Netherlands	+ 0.9	Q3	+ 1.3	+ 0.7	+ 1.8	+ 0.1	Oct	+ 2.7	Sep	6.5	Oct**	6.5
Spain	+ 3.5	Q3	+ 3.3	+ 3.4	+ 3.0	– 0.4	Oct	– 0.2	Oct	8.6	Oct	10.6
Sweden	+ 3.4	Q3	+ 3.9	+ 2.4	+ 2.8	+ 2.5	Oct	+ 7.3	Oct	5.6	Oct†	4.9
Switzerland	+ 2.3	Q3	+ 4.3	+ 1.3	+ 1.8	+ 3.9	Q2	+ 1.6	Sep	3.7	Nov†	3.9
United States	+ 3.7	Q3	+ 4.3	+ 3.6	+ 3.3	+ 1.9	Oct	+ 2.8	Oct	5.0	Nov	5.4
Euro area	+ 1.6	Q3	+ 2.6	+ 1.3	+ 1.8	+ 1.0	Sep	+ 0.4	Oct	8.3	Oct	8.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 1.9	Q3	+12.1	na	na	– 0.8	Oct	+ 5.5	Sep	8.1	Oct	8.7
Greece	+ 3.8	Q3	na	na	na	+ 3.5	Oct	+ 2.1	Sep	9.6	Q2	10.2
Iceland	+ 6.8	Q2	na	na	na	na		na		1.4	Sep†	2.6
Ireland	+ 4.1	Q2	+ 6.5	na	na	+ 0.3	Oct	+ 5.0	Sep	4.3	Nov	4.3
Luxembourg	+ 3.1	Q1	na	na	na	+15.8	Aug	+ 1.7	Oct	4.8	Oct	4.3
New Zealand	+ 2.6	Q2	+ 4.5	na	na	– 1.5	Q2	+ 4.9	Q3	3.4	Q3	3.8
Norway	+ 3.1	Q3	+ 3.2	na	na	– 4.1	Oct	+ 3.5	Oct	4.7	Oct‡	4.5
Portugal	+ 0.2	Q3	– 3.7	na	na	+ 0.7	Oct	– 0.4	Oct	7.7	Q3†	6.8

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Aug-Oct; claimant count rate 2.9% in Nov.
§EU harmonised rate 9.1% in Oct. **Aug-Oct.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Prices and wages

Dec 14th 2005
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2005	The Economist poll consumer prices forecast 2006	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 3.0	Q3	+ 2.3	+ 2.8	+ 2.8	+ 6.2	Q3	+ 6.1	+ 6.1	Q3	+ 3.5
Austria	+ 2.0	Oct	+ 2.6	+ 2.3	+ 2.0	+ 0.9	Nov	+ 5.6	+ 2.3	Oct	+ 2.0
Belgium	+ 2.6	Nov	+ 2.5	+ 2.5	+ 2.0	+ 1.6	Oct	+ 6.0	+ 2.5	Jul	+ 2.2
Britain	+ 2.1	Nov*	+ 1.5	+ 2.2	+ 2.1	+ 2.3	Nov	+ 3.5	+ 3.6	Oct†	+ 4.2
Canada	+ 2.6	Oct	+ 2.3	+ 2.4	+ 2.4	+ 1.4	Oct	+ 5.4	+ 2.2	Sep	+ 2.4
Denmark	+ 2.0	Nov	+ 1.3	+ 2.0	+ 2.0	+ 4.3	Oct	+ 3.6	+ 2.8	Q3	+ 2.9
France	+ 1.6	Nov	+ 2.0	+ 1.9	+ 1.7	+ 2.9	Oct	+ 3.5	+ 3.2	Q3	+ 2.9
Germany	+ 2.3	Nov	+ 1.8	+ 2.0	+ 1.8	+ 2.2	Nov	+ 4.1	+ 1.1	Sep	+ 1.0
Italy	+ 2.2	Nov	+ 1.9	+ 2.1	+ 2.0	+ 3.9	Oct	+ 4.4	+ 3.0	Oct	+ 2.7
Japan	– 0.7	Oct	+ 0.5	– 0.2	+ 0.3	+ 1.9	Nov	+ 2.1	– 0.1	Oct	+ 0.4
Netherlands	+ 1.8	Nov	+ 1.3	+ 1.5	na	+ 5.3	Sep	+ 6.1	+ 1.1	Nov	+ 0.8
Spain	+ 3.5	Oct	+ 3.6	+ 3.3	+ 3.1	+ 4.9	Oct	+ 5.4	+ 3.4	Q2	+ 3.1
Sweden	+ 0.8	Nov	+ 0.5	+ 0.8	+ 1.6	+ 4.1	Oct	+ 3.0	+ 3.4	Sep	+ 3.1
Switzerland	+ 1.0	Nov	+ 1.5	+ 1.3	+ 1.3	+ 1.0	Oct	+ 2.0	+ 0.9	2004	+ 1.4
United States	+ 4.3	Oct	+ 3.2	+ 3.3	+ 3.1	+ 5.9	Oct	+ 4.4	+ 3.2	Nov	+ 2.4
Euro area	+ 2.4	Nov	+ 2.2	+ 2.2	+ 2.0	+ 4.1	Oct	+ 4.1	+ 2.3	Q2	+ 2.1
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.9	Nov	+ 0.5	na	na	+ 3.3	Oct	+ 3.0	+ 3.6	Q3	+ 4.0
Greece	+ 3.5	Nov	+ 3.1	na	na	+ 6.3	Oct	+ 5.3	na		na
Iceland	+ 4.1	Dec	+ 3.9	na	na	+ 3.9	Nov	+ 6.1	+ 6.9	Oct	+ 5.3
Ireland	+ 2.6	Nov	+ 2.9	na	na	+ 0.9	Oct	– 0.4	+ 3.4	Q2	+ 4.3
Luxembourg	+ 2.5	Nov	+ 2.4	na	na	+ 2.5	Sep	+15.1	+ 1.2	Aug	+ 2.3
New Zealand	+ 3.4	Q3	+ 2.5	na	na	+ 6.1	Q3	+ 2.5	+ 3.0	Q3	+ 2.2
Norway	+ 1.8	Nov	+ 1.2	na	na	+17.9	Nov	+13.3	+ 2.6	Q3	+ 4.3
Portugal	+ 2.7	Oct	+ 2.1	na	na	+ 4.1	Oct	+ 5.3	– 0.1	Oct	– 2.4

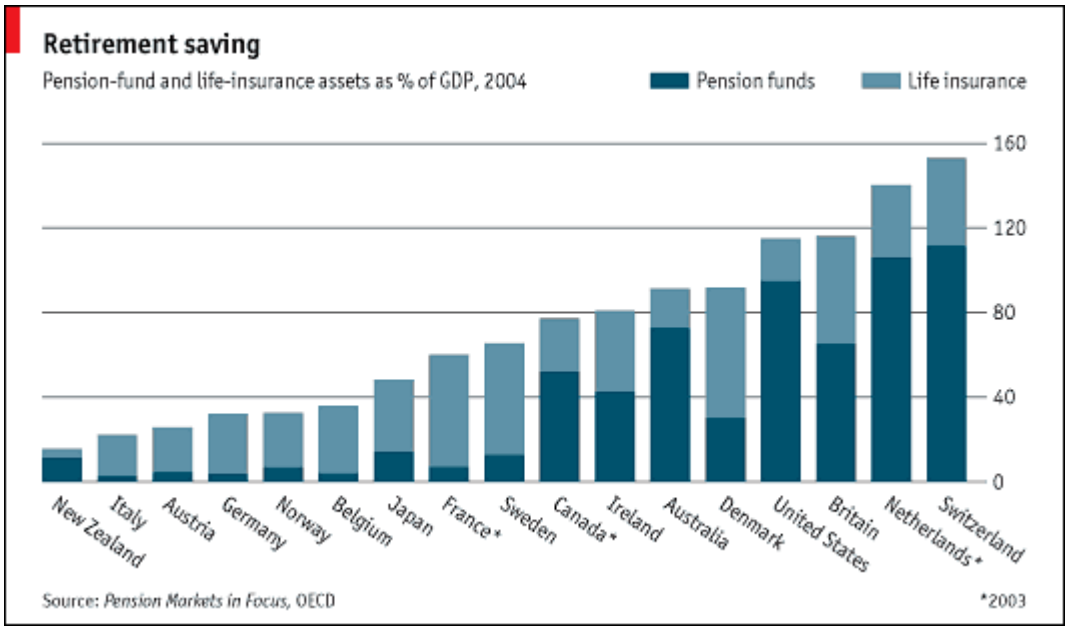
*RPI inflation rate 2.4% in Nov. †Aug-Oct.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Retirement saving

Dec 14th 2005
From The Economist print edition

Private retirement saving is carried out through both pension funds and also life-insurance companies. Some countries, including Britain, Denmark, France and Sweden, save so much with life-insurance companies that including them in the overall calculations transforms estimates of savings for retirement.



Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Money and interest rates

Dec 14th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Dec 13th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 6.5	+ 7.9	Oct	5.63	5.42	5.38	5.46	5.19	6.45
Britain	+ 5.3	+11.6	Oct	4.59	4.83	4.37	4.26	4.45	5.15
Canada	+ 7.8	+ 8.9	Oct	3.32	2.43	3.86	4.16	4.30	5.26
Denmark	+19.0	+14.1	Oct	2.45	2.25	2.84	3.34	3.70	4.92
Japan	+ 5.5	+ 2.0	Nov	0.02	0.02	0.27	1.56	1.35	1.64
Sweden	+ 4.0	+ 8.5	Oct	1.69	1.97	2.52	3.38	3.73	3.36
Switzerland	+ 4.0	+ 6.2	Oct	1.04	0.78	1.66	2.04	2.19	2.30
United States	+ 0.5	+ 7.3	Oct	4.23	2.37	4.43	4.53	4.07	5.53
Euro area†	+11.2	+ 8.0	Oct	2.46	2.18	2.79	3.37	3.50	3.82

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.72%, Japan No. 274 1.58%. Central bank rates: US fed funds 4.25%, ECB refinancing 2.25%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

The Economist commodity price index

Dec 14th 2005
From The Economist print edition

2000=100

	Dec 6th	Dec 12th*	% change on one month	% change on one year
Dollar index				
All items	139.7	143.2	+ 5.0	+17.0
Food	122.7	125.3	+ 1.9	+ 8.3
Industrials				
All	161.7	166.4	+ 8.2	+26.9
Nfa†	133.9	137.0	+ 3.2	+14.1
Metals	176.8	182.4	+10.4	+32.9
Sterling index				
All items	121.8	122.5	+ 2.7	+27.0
Euro index				
All items	109.7	110.8	+ 2.5	+30.0
Yen index				
All items	156.9	159.4	+ 5.7	+33.0
Gold				
$ per oz	507.30	537.10	+14.8	+22.9
West Texas Intermediate				
$ per barrel	59.94	61.30	+ 6.3	+46.6

* Provisional. † Non-food agriculturals.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Stockmarkets

Dec 14th 2005
From The Economist print edition

Market indices

	Dec 13th	2005 high	2005 low	% change on one week	% change on record high	Dec 31st 2004 in local currency	Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,538.7	4,617.4	3,905.5	– 0.7	– 1.7	+12.0	+ 7.8
Austria (ATX)	3,581.3	3,617.4	2,415.0	+ 0.1	– 1.0	+47.3	+29.3
Belgium (Bel 20)	3,457.9	3,464.5	2,958.8	nil	– 6.1	+17.9	+ 3.5
Britain (FTSE 100)	5,507.2	5,538.8	4,783.6	– 0.6	–20.5	+14.4	+ 5.4
Canada (Toronto Composite)	11,137.4	11,167.2	9,006.2	+ 0.4	– 2.2	+20.4	+25.3
Denmark (OMXCB)	352.4	356.8	257.8	– 1.0	– 1.2	+36.7	+19.8
France (SBF 250)	3,280.6	3,280.6	2,633.6	+ 0.4	–25.3	+24.5	+ 9.3
(CAC 40)	4,693.4	4,693.4	3,816.1	+ 0.3	–32.2	+22.8	+ 7.8
Germany (DAX)*	5,310.3	5,310.3	4,178.1	+ 0.2	–34.2	+24.8	+ 9.5
Italy (S&P/MIB)	34,972.0	34,972.0	30,645.0	+ 0.5	–30.2	+13.2	– 0.6
Japan (Nikkei 225)	15,778.9	15,778.9	10,825.4	+ 2.3	–59.5	+37.3	+17.2
(Topix)	1,626.2	1,626.2	1,109.2	+ 2.2	–43.6	+41.4	+20.7
Netherlands (AEX)	433.2	433.2	347.0	+ 0.1	–38.3	+24.4	+ 9.3
Spain (Madrid SE)	1,136.7	1,176.9	950.9	nil	– 3.4	+18.5	+ 4.1
Sweden (Affarsvarlden Gen)	286.3	286.3	218.9	+ 0.7	–28.5	+29.4	+ 8.7
Switzerland (Swiss Market)	7,577.4	7,612.0	5,669.6	– 0.5	– 9.9	+33.1	+16.9
United States (DJIA)	10,823.7	10,940.6	10,012.4	– 0.3	– 7.7	+ 0.4	+ 0.4
(S&P 500)	1,267.4	1,268.3	1,137.5	+ 0.3	–17.0	+ 4.6	+ 4.6
(NASDAQ Comp)	2,265.0	2,273.4	1,904.2	+ 0.2	–55.1	+ 4.1	+ 4.1
Europe (FTSEurofirst 300)†	1,266.8	1,267.4	1,038.6	– 0.1	–25.7	+21.6	+ 6.8
Euro area (FTSE Euro 100)†	1,074.0	1,074.0	894.4	+ 0.3	–30.7	+19.2	+ 4.7
World (MSCI)‡	1,264.9	1,264.9	1,115.0	+ 1.0	–12.7	+ 8.2	+ 8.2
World bond market (Citigroup)††	617.0	662.3	608.7	+ 0.8	– 6.8	– 7.4	– 7.4

*Total return index. †In euro terms. ‡Morgan Stanley Capital International Index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Trade, exchange rates and budgets

Dec 14th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Dec 13th	year ago	Currency units per $ Dec 13th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 15.3	Oct	− 43.5	Q3	− 5.9	− 5.3	120.0	112.1	1.33	1.31	2.35	1.58	1.10	+ 1.0
Austria	− 1.9	Sep	+ 0.2	Sep	nil	− 0.2	103.8§	104.4	0.84	0.75	1.48	–	0.70	− 2.0
Belgium	+ 15.3	Sep	+ 9.2	Jun	+ 2.3	+ 2.3	104.3§	105.1	0.84	0.75	1.48	–	0.70	nil
Britain	−115.5	Oct	− 43.6	Q2	− 1.7	− 1.9	99.7	101.1	0.57	0.51	–	0.67	0.47	− 3.1
Canada	+ 48.8	Sep	+ 19.6	Q3	+ 1.6	+ 1.6	126.3	116.1	1.15	1.23	2.04	1.37	0.96	+ 1.3
Denmark	+ 10.0	Oct	+ 9.7	Oct	+ 2.9	+ 2.6	106.0	106.8	6.24	5.54	11.0	7.45	5.20	+ 2.8
France	− 28.9	Oct	− 28.4	Sep	− 1.1	− 0.9	106.8§	107.7	0.84	0.75	1.48	–	0.70	− 3.2
Germany	+202.9	Oct	+113.6	Oct	+ 3.9	+ 3.7	104.6§	105.5	0.84	0.75	1.48	–	0.70	− 3.9
Italy	− 10.4	Sep	− 27.8	Sep	− 1.4	− 1.5	76.5§	77.1	0.84	0.75	1.48	–	0.70	− 4.3
Japan	+ 98.2	Oct	+164.3	Oct	+ 3.3	+ 3.3	80.1	88.3	120	104	212	143	–	− 6.5
Netherlands	+ 39.8	Sep	+ 44.3	Q3	+ 4.2	+ 4.2	103.8§	104.6	0.84	0.75	1.48	–	0.70	− 1.6
Spain	− 93.9	Sep	− 79.0	Aug	− 6.0	− 5.7	77.2§	77.6	0.84	0.75	1.48	–	0.70	+ 0.3
Sweden	+ 20.8	Oct	+ 24.2	Q3	+ 7.1	+ 6.5	94.9	101.5	7.91	6.70	14.0	9.44	6.59	+ 1.2
Switzerland	+ 7.0	Oct	+ 51.4	Q2	+12.5	+12.0	106.9	109.3	1.29	1.14	2.29	1.54	1.08	− 1.6
United States	−753.2	Sep	−749.7	Q2	− 6.5	− 6.5	87.3	80.9	–	–	1.77	1.19	0.83	− 3.7
Euro area	+ 47.3	Sep	+ 1.4	Sep	+ 0.1	+ 0.1	115.6	119.6	0.84	0.75	1.48	–	0.70	− 2.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 11.7	Sep	+ 8.0	Sep	na	na	81.4§	81.9	0.84	0.75	1.48	–	0.70	+ 2.1
Greece	− 34.0	Sep	− 16.5	Sep	na	na	59.9§	60.2	0.84	0.75	1.48	–	0.70	− 4.5
Iceland	− 1.3	Oct	− 2.2	Q3	na	na	106.7**	96.6	62.7	63.1	111	74.8	52.2	+ 2.0
Ireland	+ 40.6	Sep	− 3.9	Q2	na	na	94.0§	95.2	0.84	0.75	1.48	–	0.70	− 0.9
Luxembourg	− 4.5	Sep	+ 3.5	Q2	na	na	104.3§	105.1	0.84	0.75	1.48	–	0.70	− 2.3
New Zealand	− 4.3	Oct	− 8.2	Q2	na	na	142.6	134.1	1.41	1.39	2.50	1.68	1.17	+ 5.3
Norway	+ 45.9	Oct	+ 43.7	Q3	na	na	110.0	106.9	6.66	6.12	11.8	7.94	5.55	+ 15.3
Portugal	− 14.2	Aug	− 16.6	Sep	na	na	93.4**	93.6	0.84	0.75	1.48	–	0.70	− 6.0

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, October average. ‡OECD forecast. **IMF, August average.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Government budget balances

Dec 14th 2005
From The Economist print edition

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Overview

Dec 14th 2005
From The Economist print edition

In **China** the 12-month trade surplus rose in November to $102.1 billion. Growth in industrial production rose slightly to 16.6% in the year to November. It also strengthened in **India**, to 8.5% in the year to October.

Inflation slackened in **Brazil** and **Mexico**, to 6.2% and 2.9% respectively in the year to November.

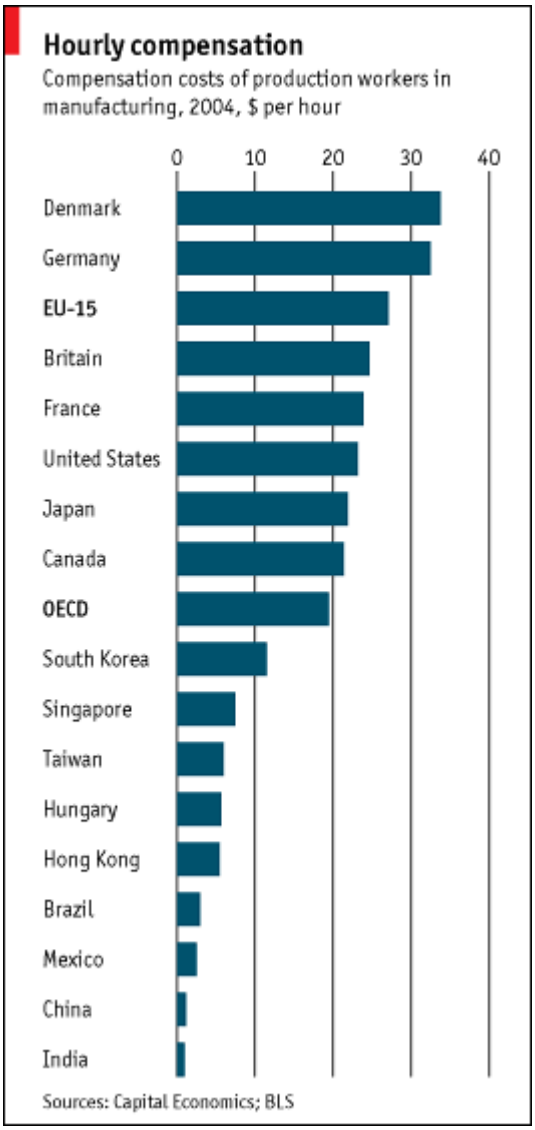
In **Turkey**, GDP growth accelerated to 7.0% in the year to the third quarter. Inflation rose slightly to 7.6% in the year to November. **Russia's** 12-month trade surplus rose in October to $119.6 billion.

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Hourly compensation

Dec 14th 2005
From The Economist print edition

American workers do not offer value for money, according to Capital Economics, a research consultancy. Their productivity, compared with rivals in Mexico, for instance, does not justify their pay. The hourly output of an American is worth $35 on average; that of a Mexican $10.25. But Americans are paid almost ten times as much. That said, American workers are better value than their overpaid rivals in Europe. German workers, for example, are paid 40% more per hour than Americans, though they produce 13% less.



Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Economy

Dec 14th 2005
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.4	Q3	+16.6	Nov	+ 1.3	Nov	+102.1	Nov	+128.5	H1	769.0	Sep
Hong Kong	+ 8.2	Q3	– 0.1	Q2	+ 1.8	Oct	– 9.0	Oct	+21.5	Q2	122.4	Nov
India	+ 8.0	Q3	+ 8.5	Oct	+ 4.2	Oct	–36.5	Oct	–16.0	Q2	136.0	Nov
Indonesia	+ 5.3	Q3	– 3.4	Sep	+18.4	Nov	+25.6	Oct	+ 4.0	Q2	31.2	Oct
Malaysia	+ 5.3	Q3	+ 4.4	Oct	+ 3.5	Nov	+25.0	Oct	+18.0	Q2	76.4	Oct
Philippines	+ 4.1	Q3	– 5.0	Sep	+ 7.1	Nov	– 1.9	Sep	+ 3.2	Jun	15.5	Nov
Singapore	+ 6.0	Q3	+17.6	Oct	+ 1.1	Oct	+16.4	Oct	+33.7	Q3	114.9	Nov
South Korea	+ 4.5	Q3	+ 8.0	Oct	+ 2.4	Nov	+25.2	Nov	+19.2	Oct	207.2	Oct
Taiwan	+ 4.4	Q3	+ 9.3	Oct	+ 2.5	Nov	+ 3.8	Nov	+ 8.9	Q3	251.8	Nov
Thailand	+ 5.3	Q3	+ 4.9	Oct	+ 5.9	Nov	– 7.9	Oct	– 3.0	Oct	48.5	Oct
Argentina	+10.1	Q2	+ 6.8	Oct	+12.0	Nov	+11.5	Oct	+ 2.9	Q2	25.7	Oct
Brazil	+ 1.0	Q3	+ 0.4	Oct	+ 6.2	Nov	+43.9	Nov	+13.0	Oct	59.7	Oct
Chile	+ 5.2	Q3	+ 4.2	Oct	+ 3.6	Nov	+ 9.2	Nov	– 0.2	Q3	16.0	Nov
Colombia	+ 5.3	Q2	+ 3.4	Sep	+ 5.1	Nov	+ 1.5	Sep	– 0.8	Q2	14.6	Nov
Mexico	+ 3.3	Q3	+ 1.0	Sep	+ 2.9	Nov	– 9.5	Oct	– 8.4	Q3	71.2	Oct
Peru	+ 5.7	Sep	+ 6.0	Sep	+ 1.1	Nov	+ 4.3	Sep	+ 0.4	Q2	12.6	Nov
Venezuela	+ 9.8	Q3	+12.4	Sep	+15.3	Nov	+28.2	Q3	+21.6	Q3	24.4	Oct
Egypt	+ 5.2	Q1	+ 3.3	2004†	+ 3.9	Oct	–10.4	Q2	+ 2.9	Q2	19.8	Oct
Israel	+ 5.7	Q3	+12.1	Sep	+ 2.7	Oct	– 7.8	Nov	+ 1.3	Q2	28.1	Nov
South Africa	+ 4.9	Q3	+ 0.3	Oct	+ 4.0	Oct	– 2.9	Oct	–10.3	Q3	17.9	Nov
Czech Republic	+ 4.9	Q3	+ 6.3	Oct	+ 2.4	Nov	+ 1.5	Oct	– 3.4	Q3	29.2	Nov
Hungary	+ 4.5	Q3	+ 9.8	Oct	+ 3.3	Nov	– 3.4	Sep	– 8.6	Q2	16.7	Nov
Poland	+ 3.7	Q3	+ 7.6	Oct	+ 1.6	Oct	– 3.2	Sep	– 4.8	Sep	39.9	Nov
Russia	+ 6.1	Q2	+ 3.5	Oct	+10.4	Nov	+119.6	Oct	+87.4	Q3	164.7	Nov
Turkey	+ 7.0	Q3	+ 7.0	Oct	+ 7.6	Nov	–42.5	Oct	–22.1	Oct	44.8	Oct
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+10.8	Q3	+ 8.7	Oct	+ 3.9	Nov	– 2.4	Sep	– 1.5	Sep	1.9	Oct
Latvia	+11.6	Q2	+ 5.8	Oct	+ 7.4	Nov	– 2.8	Sep	– 1.6	Sep	2.3	Oct
Lithuania	+ 7.6	Q3	na		+ 2.9	Oct	– 3.4	Sep	– 1.5	Sep	3.7	Oct
Slovakia	+ 6.2	Q3	+ 4.5	Oct	+ 3.3	Oct	– 1.9	Sep	– 2.6	Aug	15.1	Oct
Slovenia	+ 5.2	Q2	+ 2.0	Sep	+ 2.1	Nov	– 1.4	Sep	– 0.3	Sep	8.2	Sep
Pakistan	+ 8.4	2005†	+11.0	Jun	+ 7.9	Nov	– 8.3	Oct	– 1.5	Q2	10.0	Oct
Saudi Arabia	+ 6.2	2005‡	na		+ 0.4	Aug	+85.2	2004	+51.5	2004	29.8	Oct

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡ Forecast.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

Financial markets

Dec 14th 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Dec 13th		Dec 31st 2004	
	Dec 13th	year ago	Dec 13th	% a year		one week	in local currency	in $ terms
China	8.08	8.28	14.3	2.30	1,175.5	+2.8	- 11.6	- 9.4
Hong Kong	7.75	7.78	13.7	4.22	14,942.6	-0.3	+ 5.0	+ 5.3
India	46.1	44.1	81.5	5.64	9,263.9	+5.1	+ 40.3	+ 32.4
Indonesia	9,783	9,315	17,311	14.44	1,182.0	+5.2	+ 18.2	+ 12.1
Malaysia	3.78	3.80	6.68	3.20	898.3	+1.3	- 1.0	- 0.4
Philippines	53.6	56.3	94.9	7.88	2,099.0	nil	+ 15.2	+ 20.5
Singapore	1.67	1.65	2.96	3.19	2,324.0	+0.7	+ 12.5	+ 9.7
South Korea	1,026	1,059	1,816	4.04	1,336.5	+1.2	+ 49.2	+ 50.5
Taiwan	33.5	32.3	59.3	1.55	6,261.2	-1.4	+ 2.0	- 3.5
Thailand	41.1	39.5	72.8	4.45	693.5	+2.1	+ 3.8	- 2.0
Argentina	3.01	2.97	5.32	7.88	1,515.4	-2.8	+ 10.2	+ 8.9
Brazil	2.25	2.76	3.98	18.48	33,419.0	+0.6	+ 27.6	+ 50.6
Chile	512	581	905	5.28	9,227.6	-2.3	+ 3.0	+ 11.9
Colombia	2,275	2,379	4,026	6.39	9,038.8	+0.1	+108.0	+115.0
Mexico	10.6	11.3	18.8	8.42	17,819.7	+2.3	+ 37.9	+ 44.7
Peru	3.45	3.27	6.10	3.43	5,166.1	-0.2	+ 39.2	+ 32.5
Venezuela	2,587§	2,664§	4,578	11.50	19,773.8	-0.1	- 34.0	- 34.2
Egypt	5.75	6.21	10.17	8.81	53,052.9	+3.3	+115.8	+128.0
Israel	4.60	4.33	8.14	4.82	813.8	+1.9	+ 26.4	+ 18.8
South Africa	6.29	5.73	11.1	7.20	17,426.4	+2.4	+ 37.7	+ 23.3
Czech Republic	24.3	23.1	43.0	2.17	1,440.0	+1.6	+ 39.5	+ 28.3
Hungary	212	185	375	6.41	20,978.2	+0.7	+ 42.3	+ 21.3
Poland	3.22	3.14	5.69	4.61	34,434.3	+0.8	+ 29.3	+ 20.3
Russia	28.7	28.0	50.9	13.00	1,094.0‡	+2.0	+ 84.7	+ 78.1
Turkey	1.35	1.42	2.38	14.79	37,741.7	-3.0	+ 51.1	+ 51.3
EM (MSCI)*	1.00	1.00	1.77	na	691.4	+0.6	+ 27.5	+ 27.5
EMBI+†	1.00	1.00	1.77	na	362.9	-0.1	+ 10.1	+ 10.1

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.